Reforming multinational loggers in Solomon Islands

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By the mid-1990s, multinational loggers in Solomon Islands were working at a pace that would have depleted the commercial forests in about 13 years. The 1997–98 economic downturn in East Asia, however, has at least temporarily slowed log production, providing a window of opportunity for reformers. Since coming to power in August 1997, the government of Bartholomew Ulufa'alu has announced ambitious plans to reform forest management. This paper shows that the government has good reasons for wanting to alter the actions and impacts of multinational loggers, which includes destructive harvesting practices, tax evasion, and questionable deals with landowners. It also demonstrates that the government will face powerful obstacles as it attempts to move beyond bold declarations toward concrete changes.

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In the early 1990s, foreign timber investors —especially from Malaysia—swamped Solomon Islands, pushing log production from about 380,000 cubic metres in 1991 to over 800,000 cubic metres in 1995 and 1996. While log production in the early 1990s was only slightly higher than the theoretical sustainable yield, it had reached three times sustainable levels by the mid-1990s. At 1995 and 1996 rates, loggers would have depleted the commercial forests in about thirteen years. Since then, however, the East Asian financial crisis has contributed to a sharp drop in international timber prices and in demand for Solomon Islands logs in Japan and Korea, slowing at least temporarily this looming environmental disaster.

By November 1997, large log stockpiles —worth around SI$20 million—already existed, and production had slowed down considerably (*Pacific Report*, 10(23) 1997:2). Some foreign loggers have suspended operations and some have even considered leaving the country. The government has predicted that earnings from the forest sector will likely fall to around SI$101 million in fiscal 1998, considerably lower than the SI$319 million earned in 1997 (*Pacific Report,* 11(6) 1998:3). This is certainly bad financial news—especially considering that log exports accounted for half of total export revenue in 1996. Yet at the same time, the decrease in log production provides a window of opportunity to reform Solomon Islands forest sector, especially the effects of multinational investors.

The government of Bartholomew Ulufa'alu, which took over in August 1997, has made ambitious announcements about reforming the logging industry in Solomon Islands. The government has good reasons to push for fundamental changes, especially to the economic and environmental impacts of multinational corporate practices, which include tax evasion, destructive logging and dubious deals with landowners. Focusing on these practices also highlights some of the formidable obstacles the government faces in moving beyond bold declarations and toward actual long-term, economically viable reforms.

Background and forest policies

The land area of Solomon Islands is around 2.8 million hectares. About 85 per cent is covered by forests. Most forests are on steep slopes and small islands, and commercial logging is only appropriate or viable on about 480,000 hectares. Customary landowners control around 87 per cent of land area; the rest is owned privately or controlled by the government. In the mid-1990s, about 80 per cent of logging occurred on customary land. The main state agency responsible for forest management is the forestry division of the Ministry of Forests, Environment and Conservation. The Ministry of Finance issues log export licences and grants companies exemptions on export taxes. The Foreign Investment Board approves applications and sets minimum financial, employment, and infrastructure development criteria for foreign investors. The Division of Inland Revenue is responsible for collecting taxes. The 1969 Forest and Timber Act is the core national forest legislation in Solomon Islands. This has been amended several times and was renamed the Forest Resources and Timber Utilization Act in 1984. There are serious problems with the structure and content of Solomon Islands forest legislation: no consolidated text exists and it is often quite difficult to uncover timber management rules (see Fingleton 1989; Corrin 1992; Montgomery 1995:74–6; Ells 1996:9–11).

Serious flaws also exist with government policies to capture timber rents. Four main fees are imposed on foreign loggers: log export taxes, royalties to landowners, provincial forest charges, and corporate taxes on royalty payments and profits. During the term of Prime Minister Solomon Mamaloni from 1994 to 1997, inconsistent log export taxes, tax breaks for 'reforestation programs' and 'community development', and partial or full tax exemptions on log exports to promote processing by landowner companies (including one for the company Somma, linked to Mamaloni) have allowed companies to make windfall profits. As a result, in the mid-1990s, the government captured only a relatively small portion of timber revenues. State agencies responsible for monitoring multinational timber investors also have insufficient financial and technical resources. The Ministry of Forests, Environment and Conservation does not have enough forest officers to monitor logging sites and timber exports. The Division of Inland Revenue also has limited powers to prevent corporate schemes to evade taxes (Price Waterhouse 1995:39–40).

Multinational corporations and the state

Multinational corporations have dominated logging in Solomon Islands. Their history can be divided into three periods: 1963–81, 1981–90 and 1990–98. In the first period, three foreign loggers controlled the industry: Levers Pacific Timber, a subsidiary of United Africa Company; Allardyce Lumber Company, an Australian firm; and the US-funded Kalena Lumber Company. Levers Pacific Timber was the largest logger, accounting for two-thirds to three-quarters of total production. During this time, most logging occurred on government-owned or leased land, primarily in Western Province. Although environmental rules and management were limited, annual log production only averaged around 260,000 cubic metres, below the theoretically sustainable level.

This changed in the early 1980s. Under the first Mamaloni government (1981–84), the number of licences quadrupled and foreign firms moved into Guadalcanal, Malaita and Makira-Ulawa. Although many of these were small operations, log production escalated, especially on customary land. From 1981 to 1986, annual log production exceeded sustainable levels (based on Frazer 1997). The increase in licences and log production, the move to customary land, and the spread to more islands stretched state capacity to monitor and regulate foreign timber investors. The withdrawal of Levers Pacific Timber temporarily relieved pressure on the forests and state capacity, and aggregate production again fell below a sustainable level at the end of the 1980s.

Starting in 1991, however, an influx of Malaysian investors significantly altered the timber sector. Logging licences proliferated, often with highly favourable terms for investors. Since then many state officials have succumbed to corporate pressures (and sometimes bribes), stalling environmental reforms, eroding implementation of forest management rules, and leading to generous tax breaks. In this context, the state and communities have been even less able to monitor and control foreign loggers than in the 1980s. In 1995, log production from natural forests was 826,000 cubic metres, over twice as high as in 1991 (Solomon Islands *1996*). In 1996, despite strong domestic and international criticism, log production remained at about the same level (CBSI 1997:16). Multinational firms account for most of the log production and almost all log exports. In 1995, landowner companies only accounted for 9 per cent of log exports, and even here most had contracts with multinational firms.

Because customary landowners control most forest areas in Solomon Islands, the state has fewer legal powers to ‘manage’ commercial forests than in countries where the state owns the primary forests, as in Indonesia, Malaysia, and the Philippines. The powers that the Solomon Islands state does hold—in particular the power to regulate foreign investment and approve logging licences—had little impact on aggressive investors during the Mamaloni governments of 1989–93 and 1994–97. The process of obtaining a logging licence illustrates the constraints on, and options for, the state. To obtain a logging licence, a company first submits an application to the national government. If approved, the application is then forwarded to the relevant provincial government and Area Council. A Timber Rights Hearing, which includes landowners, Area Council members and provincial officials, determines who owns the timber, whether the owners are willing to sell their rights, how owners will share profits, and the role of the provincial government. If the parties agree to logging, a public notice must be issued with sufficient time for objections. After this, the Area Council forwards a Certificate of Recommendation and Land Ownership to the forestry division. Company officials and landowner representatives then publicly negotiate a Standard Logging Agreement (a provincial representative and a forest division representative act as observers). In theory, the forest division is supposed to monitor negotiations, ensuring that proper procedures are followed, that legal appeals are settled, and that the final logging agreement and the Area Council certificate are consistent. Assuming that the process is acceptable, the Commissioner of Forests then issues a licence to the applicant. If procedural disputes arise, or if the agreement is breached, the matter is referred to the High Court.

This process appears to provide several opportunities for the state to intervene and reject a logger's application. But in practice the government does not effectively monitor negotiations. Far too many logging licences have been approved for foreign investors, sometimes even before they make formal agreements with landowners, giving them licences without access rights. Although unlikely, if all of these licences became active, loggers could harvest four million cubic metres a year, depleting commercial timber in only three years (Economic Insights 1994:54; Baird 1996; Ells 1996:10–11).

Landowner and corporate negotiations for timber rights and licences are often long and acrimonious. Although delays have frustrated some investors, inadequate state supervision, ambiguous laws, corrupt and divided community negotiators, corporate bribes, corporate funding of Area Council (Timber Rights) meetings, and highly trained corporate negotiators have generally allowed multinational timber companies to negotiate favourable agreements. For example, the Standard Logging Agreement and the Forest Act recommend a royalty rate of 17.5 per cent of free-on-board (f.o.b.) value. Yet the average royalty rate in 1994 was only 11.5 per cent of f.o.b. value. Moreover, despite favourable agreements, timber investors have distorted or broken many agreements with landowners. They have ignored verbal or written promises to provide 'lasting development', such as roads, bridges, medical clinics, or schools. They have often left behind far more damage than landowners expect, disrupting traditional food sources, polluting rivers and violating sacred sites. And they have evaded timber royalty payments (Bennett 1995:262; Frazer 1997:51; Price Waterhouse 1995:23; Ells 1996:11, 16, *Sol-Tree Nius* 2 (February) 1995:3; Fingleton 1994:21).

Corporations have also pressured and bribed some key politicians and bureaucrats to create a favourable policy climate for investors and reverse reforms that threaten profits. The most visible example occurred during Prime Minister Billy Hilly's government from 1993 to 1994. The Hilly government initiated reforms to lower log production and strengthen state control over foreign timber investors. The government raised log export taxes, and increased efforts to verify log export prices, grades, and species. The government also began work on new national forest legislation, proclaimed plans to ban log exports in 1997, and floated the idea of hiring a foreign company to strengthen surveillance and compliance. These moves to control timber investors were quickly thwarted. In October 1994, Hilly's government fell after a series of defections and resignations. According to former Minister of Forests, Environment and Conservation Joses Tuhanuku (1993–94), this was 'the making of foreign logging companies' (Tuhanuku 1995:69). From 1994 to 1997, environmental protection and control over foreign investors weakened even further under Prime Minister Mamaloni. The government decreased log export taxes, postponed the log export ban until at least 1999, removed foreign advisers, abolished moves to strengthen surveillance of foreign operations, and agreed to cancel four forestry aid projects, including the Timber Control Unit Project (created in 1993 with the support of Australian aid to monitor log grades, species, volumes and prices).

Foreign loggers have largely ignored environmental rules outlined in Standard Logging Agreements. In theory, companies must supply landowners with logging and road plans, obey the River Waters Act, follow proper skidding practices, clean up work areas, restrict logging to safe distances from waterways and to stipulated species and sizes, follow cutting and removal rules, and construct roads and bridges according to government guidelines. Some corporate groups, such as Malaysia's Kumpulan Emas, have little logging experience. Others, especially from Sarawak Malaysia, have terrible records at home (Dauvergne 1997a:Chapter 4). In Solomon Islands, weak state administrative capacity, limited state legal powers, remote logging sites, and few provincial and community resources allow loggers to operate with little scrutiny and almost no restraints. Tuhanuku writes: 'During my time as Minister, foreign logging companies persistently showed a blatant disregard for the nation's laws, regulations and policy of the government of the day' (Tuhanuku 1995:69). Companies log areas outside their licence, damage or cut undersized and protected trees, build temporary and inappropriate roads and bridges, leave pools of stagnant water that spread malaria, pollute and disrupt food and water sources, disregard reforestation duties, and ignore obligations to consult with landowners. A study of a logging site operated by the Malaysian company Silvania concluded 'the degree of canopy removal and soil disturbance was the most extensive seen by the authors in any logging operation in tropical rainforest in any country' (quoted in Forests Monitor 1996:7). Montgomery argues that

> to come back and re-cut the Solomons forest in 50 years and get equivalent sorts of yields to what they are now producing means that everything has to be done correctly now. The reality is that there is no adherence at all to a silvicultural regime that will allow this to occur. Many of the harvesting operations are still poorly planned and poorly managed (Montgomery 1995:74).

The *1995 Forestry Review*, an unofficial internal government document, is even harsher: 'forest practices in many locations [in Solomon Islands] are amongst the worst in the world' (see also South Pacific Regional Environment Programme 1992:25–6; Greenpeace Pacific 1995).

Besides dismal environmental practices, foreign loggers have pressured and enticed state officials to provide generous tax breaks. For example, the *Solomon Star* reported that from 1993 to 1995 Integrated Forest Industries distributed SI$7 million and supplied generous perks to government ministers and powerful bureaucrats. Not surprisingly, Integrated Forest Industries paid no taxes in 1995. In that year, according to the *1995 Forestry Review*, as a result of tax breaks combined with lower international prices and lower export taxes, government revenue captured by the log export tax fell by SI$12.6 million, even though log exports jumped by 88,000 cubic metres.

Securing tax breaks is only one means that loggers use to increase and maintain profits. They also evade royalty payments, log export taxes and corporate taxes on profits. Companies forge the names of species and log grades, conceal high-grade logs in low-grade shipments, and simply under-record prices to lower log export taxes (which in turn lowers recorded profits). According to Duncan, schemes to under-record log export prices in 1993 may have cost Solomon Islands government up to SI$94 million (Duncan 1994:xvii). Price Waterhouse estimates that 'the declared f.o.b. value is...25 per cent to 30 per cent under-recorded' (Price Waterhouse 1995:ii). The *1995 Forestry Review* claims that most firms 'should have at least been able to achieve the prices realised by Somma of SI$458 as the Makira logs are generally smaller and of lower quality to those on other concessions'. (Somma had less incentive to under-declare log export prices because the government exempted it from 96 per cent of the log export tax.) Yet in 1995, all foreign loggers reported far lower average log export prices than Somma, decreasing the overall average export price to a mere SI$366. A 1995 report by Solomon Islands Central Bank and the Timber Control Unit also uncovered evidence of underpricing of log exports. After calculating for reasonable shipping and insurance costs, this report found that the average Japanese import price of Solomon Islands logs in 1994 was US$33.90 per cubic metre higher than the declared export price; in Korea, it was US$32 per cubic metre higher (agent fees in places like Singapore and Hong Kong may account for about US$5 of the difference, Mulholland and Simbe 1995:2).

According to a general manager at one of the largest foreign timber companies in Solomon Islands, timber operators also make informal agreements with traders for guaranteed log purchases (interview, Honiara, 11 July 1996). Solomon Islands customs data seems to confirm that these arrangements are pervasive. Data from July 1993 to May 1996 shows that the Australian company Allardyce sold more than 98 per cent of its logs to Itochu corporation while the mainland Chinese company Dalsol sold all of its logs to Zhong Xing Investment. From January 1994 to May 1996, the Malaysian company Kalena Timber sold all of its logs to Durley Holdings Ltd in Singapore. Other foreign and local loggers also have strong ties with one or several buyers (Dauvergne 1997b). Such deals help loggers to maintain steady production, provide some insurance against price fluctuations, and in some cases, furnish loggers with essential credit or technical assistance to maintain operations. However, they also tend to push up aggregate production levels, depress log export prices by severing competitive bids, and facilitate transfer pricing and tax evasion.

Resistance and reforms

In short, serious environmental and financial problems plague the commercial timber industry in Solomon Islands. The Ulufa'alu government needs to consolidate and strengthen forest and environmental legislation. It needs to cut the number of timber licences and facilitate stronger and more advantageous contracts between landowners and timber firms. The government needs to bolster efforts to ensure that companies actually meet obligations to protect the environment, provide lasting community development, and obey the regulations in Standard Logging Agreements. The government also needs to improve the amount of revenue captured from timber investors, through both reforming policies and strengthening enforcement. It needs to crack down on tax evasion, transfer pricing, and the informal agreements among companies within corporate groups and between investors and corporate buyers. It is equally critical to overcome corporate pressures, threats, and bribes that have contributed to generous tax breaks (which have in turn stimulated unsustainable logging as companies pursue windfall profits). This is undeniably a difficult task. At the moment, state agencies do not have adequate technical, human or financial resources. Problems at some agencies, such as the Division of Inland Revenue, are compounded by insufficient powers to monitor and control sophisticated multinational investors. Reforms are hampered further by the complexity of landownership arrangements and overlapping and unclear responsibilities for timber management. Moreover, the government must remain constantly vigilant to avoid succumbing to corporate bribes and gifts, such as happened to Hilly's government in 1994.

Despite these difficulties, there are some reasons for optimism. Supported by local non-governmental organisations , a broad social base of opposition to loggers appears to be gaining strength (Frazer 1997:54–60; Roughan 1997). Some angry opponents have even sabotaged equipment and burned logging camps (Friesen 1994:29; personal communication, Tarcisius Kabutaulaka, May 1998). To some extent, this has slowed and restricted corporate expansion. Although general opposition, pressure from non-government organisations, and local anger are not yet strong enough to force major changes to corporate practices, this does provide an opportunity for the Ulufa'alu government to work with non-government organisations and disgruntled communities, thereby increasing government leverage.

Since August 1997, the Ulufa'alu government has made ambitious announcements about reforming the commercial timber industry. So far however, markets, not government actions, have driven most of the concrete changes, and already signs are emerging that the government is unable or unwilling to implement some of these pronouncements. In late 1997, the government revoked all exemptions and discretionary remissions of duties. Yet by April 1998 the government had retreated, granting a 50 per cent exemption on log export taxes (pers comm, John Naitoro, April 1998). The government also declared in late 1997 that the annual log production target would be lowered to about 400,000 cubic metres. Yet it is unclear whether the government can actually control production volumes on the ground. The target appears to be mostly an opportunistic statement that simply reflects current market demand. If demand and prices rise, log production in Solomon Islands could well rise again to reflect these market changes.

The government also announced in late 1997 plans to establish over the next twelve months an auction system to sell logs. This would require buyers to purchase logs or sawn timber at auctions held four times a year at two sites (one in Western Province and the other in the eastern part of the country). These sites would also have sawmills to process logs rejected by overseas buyers. The government hopes that auctions will compensate for lower volumes. As Prime Minister Ulufa'alu noted in November 1997

> at present we have no way of knowing the truth about the price the loggers are really getting at the end of the day. But if people are coming over once every three months to the auction, to bid for logs, then definitely we will get a better price and that will compensate for the lower volume (*Pacific Report*, 10(19) 1997:5).

Putting aside a discussion of the merits and feasibility of this proposal, it seems highly unlikely that the government could set up an auction system within a year. The government will also likely face direct and indirect attempts by corporations to scuttle these plans.

The Ulufa'alu government does appear committed to reforms and further changes could still occur. The government has reinstated the Timber Control Unit and placed a moratorium on new licences. The Ministry of Forests, Environment and Conservation is currently reviewing and attempting to consolidate and reform forest legislation, including the Forest Resources and Timber Utilization Act, the Environment and Conservation Bill, and the Wildlife Bill. It is also working on improving enforcement and monitoring, and strengthening the penalties for illegal and destructive activities. In addition, it is trying to collect more accurate statistics, including an estimate of the remaining volume of commercial timber. Hilda Kari, Minister of Forests, Environment and Conservation, stated on 20 April 1998 during the debate on the budget that her ministry now recognises that the Forest Resources and Timber Utilization Act had 'outlived its usefulness'. She also announced that her ministry would 're-visit all existing licenses, whether local or foreign owned'. She argued that 'the only way for this country to move forward in the right direction is to cancel all licenses that are not doing any reforestation'. She noted that numerous landowners had applied for felling and milling licences, even in areas where foreign loggers are now operating. She argued that this is often in response to the perception of unfair deals and she vowed that the government would examine all licences and rectify any injustices. In addition, she declared that her ministry 'recognises the need for the industry to be localised', although at the same time she also noted that landowners need capital, equipment, and training to conduct logging (Kari 1998).

In this speech, Kari was highly critical of the actions and impacts of multinational loggers. She argued that 'our resources have been tapped by others who have only given us the crumbs as it were, by royalty payments, technology agreement, profit sharing arrangements and so on.' Later in her speech, she declared that

> as much as the present Act enables foreign investment, I wish the new Act must re-orientate/redirect foreign investment to encourage downstream processing in the timber industry and in value-added activities. At the same time, it is the Government's desire for resource owners to take control of harvesting of forest resources so that the statement that resource owners must get maximum benefit is real (Kari 1998).

She went further and noted that even though the government will continue to encourage 'good foreign investment in the forest sector…it is only common sense to reduce foreign owned logging companies in order to accommodate our own local owned companies' and remain within sustainable production levels (Kari 1998).

As of early June 1998, then, it is still too early to know how extensively the Ulufa'alu government will reform specific forest policies and practices. It is also difficult to predict the future path of logging in Solomon Islands. What does seem certain, however, is that government moves to reform the actions and impacts of multinational timber companies will face formidable hurdles. Moreover, if market conditions improve, the government will have to remain vigilant and determined to avoid drifting back on to the path of destructive and unsustainable logging.

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