

The Logging Sustainability Committee

Report Background Information

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The Logging Sustainability Committee Report to Cabinet

1. Introduction

The Sustainable Logging Committee was established in mid-April 2018 in the midst of concerns surrounding the possibility of export receipts no longer being facilitated by Pan Oceanic Bank, which facilitates receipts for a large majority of the logs exported from the country.

The Sustainable Logging Committee was tasked to provide policy directions to ensure a long-term solution to the current unsustainable logging sector practices. It was also expected that as the core Ministries are represented on the Committee, the Committee would provide a mechanism to coordinate work on the current issues facing the logging sector related to the banking sectors facilitation of logging receipts.

The Sustainable Logging Committee was tasked to submit their Report to Cabinet by the end of June 2018.

Terms of Reference Logging Sustainability Committee

- 1) developing a **Logging Sustainability Policy**, which includes a range of initiatives aimed at putting logging on a sustainable path;
- 2) designing an **Expenditure Strategy** on how the Government can revise expenditure expectations to match the likely reduced revenue collected from lower log exports in future years; and
- 3) formulating **Recommendations** on complementary measures that the Government could consider implementing in terms of:
 - A) social cohesion and education on logging sustainability in the Provinces; and
 - B) promoting alternative sources of growth and livelihood opportunities in the Provinces.

2. Overview

Solomon Islands – logging as a key contributor in the economy

Logging has been the key sources of Government revenue and foreign exchange since the 1990s.

As of 2017, the revenue from logs accounts for around 20% of the Government domestic-sourced revenue. Although, it is a main revenue source, the administration of the sector is weak and the magnitude of harvesting far exceeds the sustainable level. Hence, the need to review and redirect the policy to address the regulations and practices in the right direction that will improve government revenue collections from a sustainable forest resource over time and space. This will require collective action from relevant Government agencies and other stakeholders. The intention of this paper is to identify areas that needs to be the focus of future initiatives to ensure the harvesting of logs is done in a sustainable manner and in accordance with the required standards.

The Solomon Islands Democratic Coalition for Change Government is committed to sustainable logging practices in Solomon Islands and this includes a suite of measures to place logging on a more sustainable path for the wellbeing of the Solomon Islands’ environment, people and economy.

Solomon Islands faces many challenges to its growth trajectory, such as a high population growth rate, large distances from key trading markets and being geographically dispersed across many Islands from East to West. As the country plans for graduation from the group of countries considered to be Least Developed Countries (LDCs) by the United Nations, it is important the country carefully considers its future growth plan and strategically prepares to optimise the use of the scarce and valuable resources with which we are naturally endowed, such as the forestry sector.

Against this backdrop of planning for the future, **Solomon Islands need to be mindful of the lingering vulnerabilities that exist. The country is forecast to experience modest real growth of around 3% over the medium term,** however, with a high population growth rate of around 2.7% – **this means minimal improvements in living standards for its people.** This growth challenge facing the country not only requires better management of current

resources, it demands new sources of growth and resilience to be promoted and investment in core infrastructure – such as energy and telecommunication - to support growth activity.

Solomon Islands currently relies on the forestry sector as a key contributor to government receipts, exports and growth - with receipts from logging accounting for around 20 per cent of government revenue and accounting for around 65 per cent of the total value of exports from the country. **Payments of royalties to resource owners also provides a source of revenue to rural communities** where a majority rely on subsistence living, there is limited basic infrastructure, and they are located long distances from urban areas.

The need for change – putting logging on a more sustainable path

The Solomon Islands Democratic Coalition for Change Government recognises the need for action to put logging on a more sustainable path to ensure benefits for future generations.

While a reduction in the volume of logs being harvested may have a direct impact on government revenue in the short-term, it will be important that the country gets more from the resources it exports counterbalancing some of the revenue loss left by the reduction in exports. It is vital that logging volumes decrease from the current high unsustainable rate to provide for a more sustainable revenue source into the future, as opposed to the depletion of a renewable resource.

The Sustainable Logging Policy includes key priority areas of focus of further work to put harvesting of the commercial trees in our island forests on a more sustainable and environmentally friendly path and to ensure a greater and sustainable return into the future.

Key areas include:

- Improved enforcement of current rules;
- Initiatives to encourage sustainable harvesting and environmentally beneficial activity and encourage over-logged forest rehabilitation initiatives;
- Socially responsible industry participants;
- Minimising misclassification of round logs exports; and
- Enhanced downstream processing outcomes.

The impacts on the economy will guide the implementation of the new **Sustainable Logging Policy**. The transition to more sustainable logging practices will need to be a phased approach to limit impacts on economic stability and minimise severe shocks which would ultimately affect growth and development in the country, have a detrimental impact on the business community and the living standards of Solomon Islands' people.

The Solomon Islands Government is committed to get a greater return from a more sustainable export of logs. The Government wants to work hand-in-hand with the Solomon Forest Association to ensure genuine, financially viable companies that own their own logging machineries and equipment and companies of good character and standing are operating in the forestry sector. Likewise, consultations have been conducted with the Sawn Timber industry associations to gather their input in terms of generating greater returns from downstream processing of timber with added values.

Ensuring greater transparency and accountability for actions in the forestry sector is to ensure the appropriate management of our natural resources, but also to ensure the Government is accountable for its role in the managements of the nation's natural resources, and the industry is accountable for its actions. This action aims to ensure that current risks emanating from the forestry sector are minimised for the benefit of the country's future growth and prosperity.

3. Update: US corresponding bank and export receipt facilitation

Update

POB's loss of its US dollar corresponding bank

In October 2017, the Pan Oceanic Bank's (POB) corresponding US dollar denominated bank ceased facilitating logging receipts. Most logging receipts are currently facilitated by POB.

Since that time, POB has struggled to find a bank willing to be their corresponding US dollar denominated bank to facilitate export receipts (the last time they had to find a new corresponding bank, it took around 9 months). Much of the unwillingness of international banks to fill this role is due to possible counter-terrorism financing and anti-money laundering (CTF-AML) concerns.

Most recently, POB has entered into discussion with a UK Bank to be their US dollar corresponding bank. These discussions are still ongoing. POB has also sought assistance to improve practices and resolves CTF-AML concerns that led to the previous banking relationship breaking down.

Since October 2017, CBSI has helped with the facilitation of the export receipts through their central bank operations with the Federal Reserve Bank of New York (FRBNY). However, as these are commercial transactions, the FRBNY has given notice that it will stop facilitating these payments at the end of December 2018, a deadline which has previously been extended from June 2018.

Other commercial banks facilitating payments

The Logging Sustainability Committee has held consultations with one other commercial bank to ascertain the likelihood of these other commercial banks taking on log exporters as new customers and facilitating their export receipts.

While BSP does currently have two logging companies as current members, these members have been long-time customers of the bank when it was formally National Bank of Solomon Islands. The Bank faces strict limitations imposed by major shareholders that limits the amount of business they can facilitate related to logging. Likewise, there are broader concerns in regards to sustainability of the industry, the enforcement and adherence to

forestry rules and standards, environmental impacts, impact on communities, and the social corporate responsibility of companies involved in logging, which all need to be considered before any additional logging companies could join the bank. The Committee was informed that there would need to be a substantial shift in the current undertakings of the industry and demonstration of sustained bolstering of the regulatory environment in regards to enforcement of rules and ensure compliance by companies, before BSP could even consider new members from the forestry sector.

Concerns about the beneficial ownership and transparency of international payments is paramount in the post-September 11 environment

The counter terrorism financing and anti-money laundering (CTF-AML) regime aims to tackle money laundering — involving profit-making crime (such as corruption, drug trafficking, market manipulation, fraud, tax evasion) — along with preventing the financing of terrorism activity. Transparency is paramount to ensure that the flow of funds can be traced and the ‘true’ owners of money and assets can be identified.

AML/CTF controls, when effectively implemented, mitigate the adverse effects of criminal economic activity and promote integrity and stability in financial markets. Globally there has been a push to implement strong AML/CTF controls, particularly since September 11 terrorist attacks.

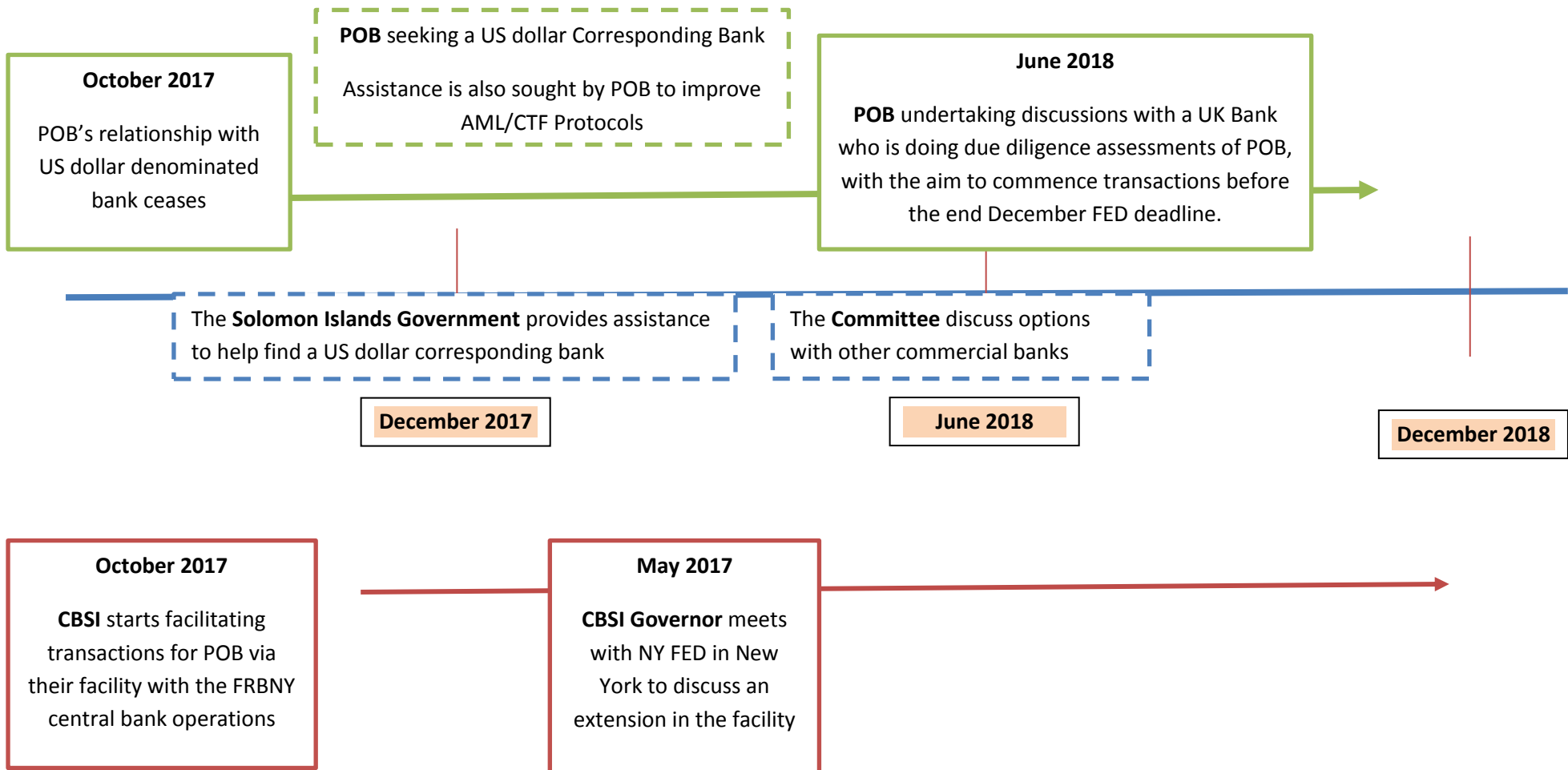
AML/CTF controls have had a detrimental impact on remittance flows as recipients of remittances in developing countries are sometimes unable to clearly identify themselves, which is a requirement under the AML/CTF rules.

Unsustainable logging cannot be supported from a corporate social responsibility perspective

Corporate Social Responsibility, is a corporation’s initiatives to assess and take responsibility for the company’s effects on environmental and social wellbeing. The term generally applies to efforts that go beyond what may be required by regulators or environmental protection groups. Many corporations, particularly those that are international publicly traded companies, have strong Corporate Social Responsibility policies which limit the type of activity they can engage in.

The unsustainable nature of logging in Solomon Islands, means that many organisations, including commercial banks, would be unlikely to want to be linked to the activity unless it was done on a more sustainable basis.

Banking Facilitation of Logging Receipts: Timeline of Events



Worst Case Scenario – All Logging Activity Ceases after 31 December 2018

Situation: In the worst case scenario, being that the facility between CBSI and the FRBNY ceases at the end of December 2018 and POB has not established a US dollar corresponding bank, a majority of logging activity would cease as payments for export receipts will not be facilitated.

Modelling by MoFT has found that under the worst case scenario (all logging ceases):

Real GDP Growth	-8.9%	*The decline in real GDP would be long lasting as it represents real lost growth for the country and a worsening of living standards. It is estimated to take 4 years before GDP is back to 2018 levels.
Domestic Revenue	-\$660m + second round impacts adding at least another \$150m in lost revenue	<p>*Direct revenue impact from the reduction in export revenue is due to no log exports. *Second round impacts also impact on revenue as there is reduced spending from the decreased forestry related activity and income in the economy:</p> <ul style="list-style-type: none"> • Reduced PAYE. • Reduced Royalties. • Reduced overall spending on goods and services. <p>Based on 2017 employment data, logging industry provided around 10,000 jobs, both skilled and unskilled workers. This represented around 20% of total employment.</p> <p>*This would be a permanent decrease in the level of Government revenue being generated, with future revenue increase reliant on growth and agreed policy measures.</p>
Export Growth	-66.3%	*As logs account for around 66% of the value of all export, total exports will be severely depleted with the ceasing of logging activities, which impacts directly on the Balance of Payments (BoP).
Foreign Reserves	5.3mths	*Foreign Reserves would drop to 5.3 months of import coverage by the end of 2019 and continue to decline instigating a BoP crisis as there is insufficient foreign reserves from export activity to pay for imports.

4. State of the Forest Report

The most recent formal inventory assessment of the Solomon Islands Forestry Sector was in 2011, conducted by Sinclair Knight Merz (Solomon Islands National Forest Resources Assessment: 2011 Update). Since that time, drone analysis has been completed to provide a topographical estimate of the change in the Forestry inventory.

While Solomon Islands supports an extensive cover of natural forest, only about 30% of the land area (~800,000 ha) was assessed in previous resource assessments to support forests that are suitable for commercial timber production.

The largest tracts of commercial natural forests are located in Western, Isabel, Guadalcanal and Choiseul provinces. Industrial plantations comprise of less than 36,000 ha in total and are largely confined to the Western Province. Individuals and community owned plantations across the country amounts to around 10,000 hectares.

The unprecedented high rates of logging since 2005 have been sustained by continued utilisation of primary or undisturbed forests, including areas that were previously assessed not to be suitable for commercial production and some that are outside of current logging licence boundaries. Logging has also taken place in natural forests that have previously been logged (secondary forests). This project estimates that logging has taken place on 348,000 ha of primary and secondary commercial forest since 2006 and on almost 17,000 ha of non-commercial forest.

In 2011, Approximately 325,000 ha of primary commercial forest was estimated to remain unlogged.

The analysis of forest resources across the country using Collect Earth and satellite images on 2km x 2km plots concluded that around 22% of the 90% forest cover is accessible production natural forests. About 17% of the production forest had been logged and 85% of the active felling licences are currently logging the regenerated logged over forests. The remaining 5% of the production forests are still virgin and will be logged out in the next 5 years. Most of these forests are in the Choiseul Province.

Findings from the 2011 Assessment

Findings from the 2011 Assessment was that with continued, short-cycle logging of secondary forests it may be possible to sustain relatively high rates of log exports from Solomon Islands through to the end of the 2020s and log exports from at least Western and Choiseul Provinces for at least a further decade.

While this pattern would sustain SIG revenues and logging-sector employment for two to three decades, it is anticipated to irreversibly degrade the productive capacity of the commercial forests and greatly diminish the value of ecosystem services they provide (e.g. biodiversity, watershed protection, provision of food and traditional medicines, cultural heritage).

Given the significant increase in log exports since 2011, outcomes under Scenario B are likely to be reached much sooner.

It is expected that given the actual exports since 2011 have been much higher than Scenario B (Business As Usual Scenario) anticipated, that the ‘drop off’ point in terms of logging inventory has likely been pulled forward.

Plantation logs to fill the gaps left by commercial forest

The report also found that the plantations sector, if maintained, has potential to sustain employment and land owner income following the anticipated decline in the natural forest sector during either the 2025-30s (if a sustainable harvest cycle is adopted) or 2050s (onward; when commercial natural forests are largely exhausted). However, as log exports from plantations are not subject to export duties, they will not help to directly fill projected gaps in SIG revenue.

Possible Scenario Comparisons

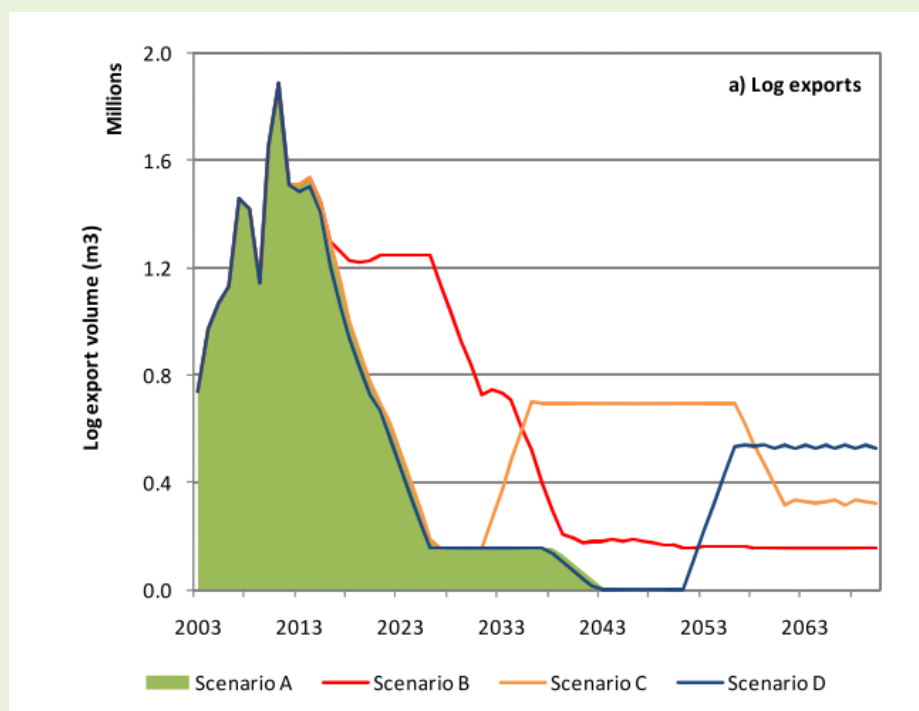
A woodflow model was developed to assess the impacts of future logging activities on Solomon Islands forests. Four scenarios were developed to assess future woodflows and associated revenues for SIG:

- **Scenario A: One-off utilisation of the primary and current secondary commercial forest area:** in this scenario logging continues in each province at the average rate for 2006-2011, until the entire primary commercial forest and all pre-

2006 secondary commercial forests are fully logged. Following completion of this cycle of logging, there is no further logging in secondary forests.

- **Scenario B: Market driven business as usual logging:** in this scenario logging takes place with little effective control until Solomon Islands' commercial forest resources are exhausted. Logging continues in each province at the average rate for 2006-2011, drawing on remaining primary forests, secondary forests and accessible marginal forest areas. Re-entry logging in secondary forests continues on a 10 year cycle until forest productivity diminishes to very low levels.
 - **This scenario is representative of what has been experienced in the years since 2011, however, the volume harvested has been much higher than forecasted.**
- **Scenario C: Later re-entry into recovering forests:** this scenario follows Scenario B, except that after utilisation of the current primary and secondary forest resource, timber production in the subsequent secondary forests is managed on a 25 year harvest cycle.
- **Scenario D: Sustainable rotation:** in this scenario timber production moves to the minimum harvest cycle considered to be necessary for sustainable rotations in tropical rainforests (45 years). Yield and log composition in secondary forests are similar to those in primary forests. There is no further logging in non-commercial forests.

Chart 1: Scenario Comparisons – Yearly Log Exports



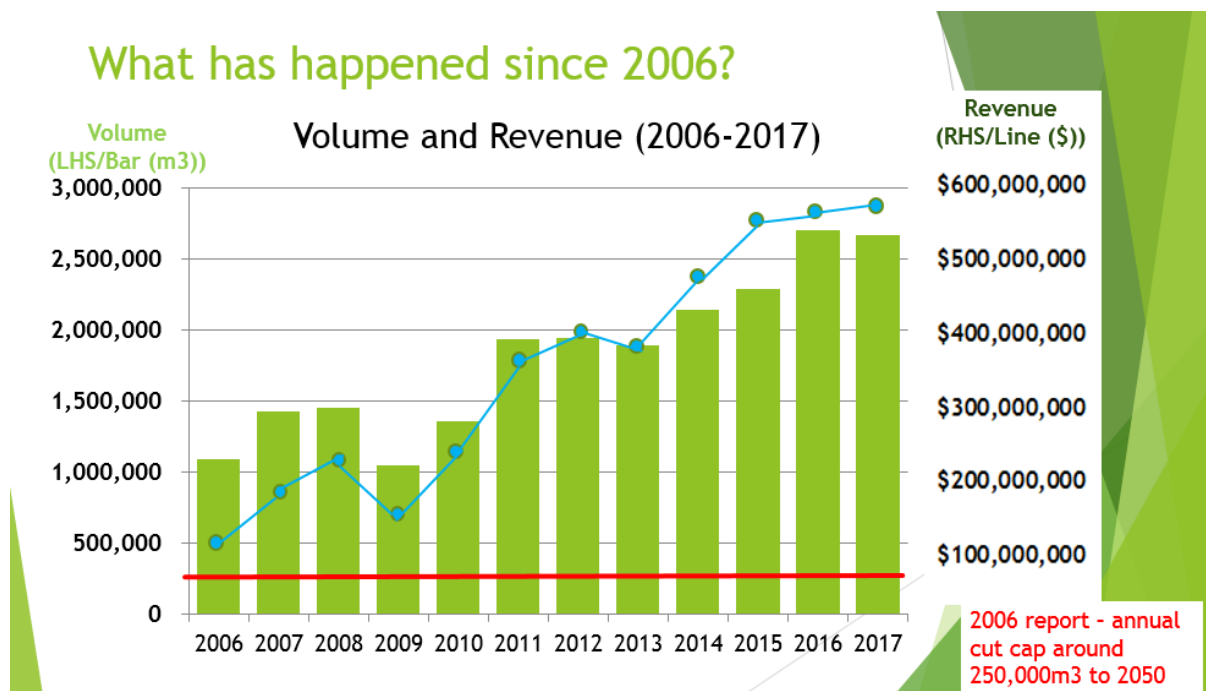
Source: SKM Solomon Islands National Forest Resources Assessment: 2011 Update

Logging Exports since 2011

Since 2011, the volume of logs exported has dramatically increased. **In 2006, the sustainable harvest amount was estimated to be 250,000m³.** Since 2011, a total of 15.5 million cubic meters of round logs have been exported from Solomon Islands, with exports increasing from just under 2 million cubic meters in 2011, to be on track for 3 million being exported this year, 2018.

Since 2006, the export duty charged per cubic meter has gradually increased, as the Determined Value Schedule (which is used as a proxy for the value of logs being exported to set the export duty price), was gradually increased to be on par with international market prices.

Log Volume and Export Duty Revenue (2006 – 2017)

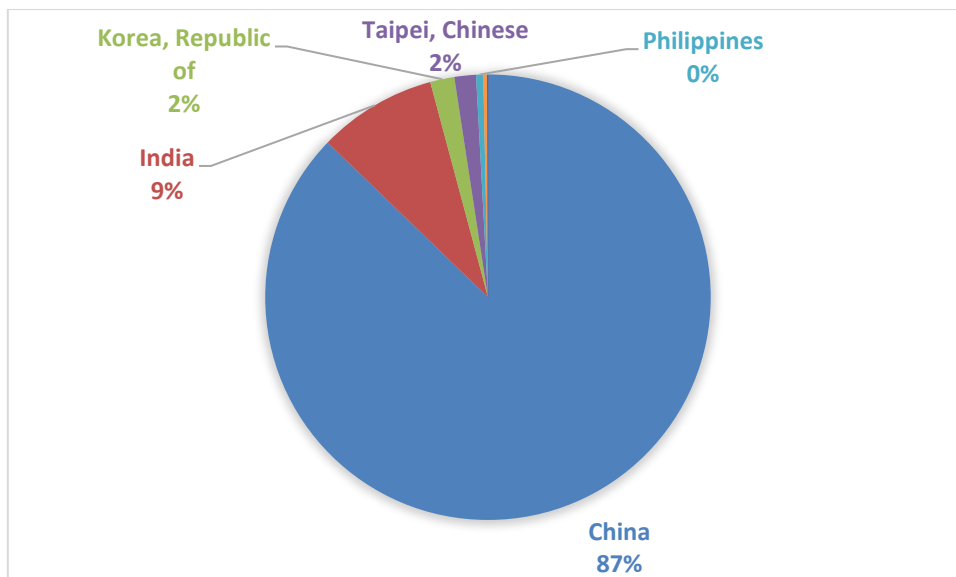


Source: Solomon Islands Customs Data

China dominates the export market for round logs

In terms of the destination markets for Solomon Islands' round logs, 87 per cent of logs went to China in 2017, with a further 9 per cent recorded as going to India.

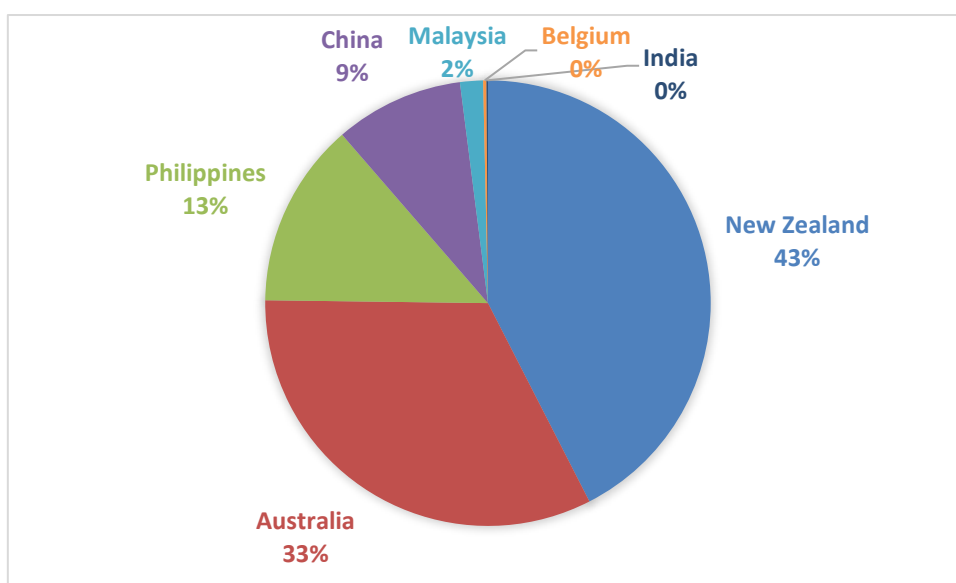
Destination of Round Logs exported in 2017



Source: International Trade Centre & UN COMTRADE

Unlike round logs, sawn timber exported from Solomon Islands mostly goes to Australia and New Zealand. Most Rosewood goes to Australia, while a majority of sawn timber to New Zealand is Vitex for decking.

Destination of Sawn Timber Exports in 2017



Source: International Trade Centre & UN COMTRADE

Current Logging activity by Province

Active Felling Licences in 2017 and 2018

<u>Province</u>	<u>2017 Total</u>	<u>Active Felling Licences 2018</u>			
		<u>Quarter 1</u>	<u>Quarter 2</u>	<u>Quarter 3</u>	<u>Quarter 4</u>
1. Western	77	38			
2. Choiseul	47	30			
3. Isabel	42	26			
4. Malaita	51	13			
5. Guadalcanal	31	20			
6. Makira	33	20			
7. Renbel	4	4			
8. Temotu	6	3			
9. Central	4	3			
Total	295	157			

The table above summarises the total felling Licences issued and renewed in 2017. However, in 2018, Quarter 1, only 157 felling Licences were active and 138 were dormant. Most of the felling Licences have logging concession areas in the Western Province (24%), second Choiseul Province (19%) and third Isabel Province (16%) for the last 3 years.

The Ministry still implements the moratorium provided for by LN 114 endorsed by Cabinet in 2007. Currently 74 SFA members that are foreign owned are operating in the Solomons. Around 10 companies operating are locally owned.

Round Log Export Summary (Forestry data)

<u>Province</u>	<u>Volume (m³)</u>		
	<u>2016</u>	<u>2017</u>	<u>2018 (Jan-Apr)</u>
Western	837,765.773	946,865.000	284,048.0
Isabel	560,272.452	687,868.000	255,890.0
Choiseul	353,789.000	563,888.732	207,202.0
Guadalcanal	331,655.000	501,873.000	150,784.0
Malaita	248,625.005	197,600.000	71,760.0
Makira	112,395.000	207,936.000	94,248.0
Renbel	211,450.000	162,800.000	69,500.0
Temotu	55,870.000	80,700.000	58,316.0
Central	25,623.000	52,809.000	27,200.0
	2,737,445.230	3,402,339.732	1,218,947.0

The industry is on track to reach a staggering 3 million m³ in 2018 if nothing is done

- Western, Isabel and Choiseul are still the top Provinces that hosted logging industry for the 3 years
- Forestry declared a volume of 1,218,947.0 m³ for Quarter 1 (Q1) 2018
- Possible that log export will reach above 3.0 million m³ in 2018
- Customs Division/Ministry of Finance declared a 30% increase in the quantity of exports of round logs in Q1 2018 compared to same period in 2017.
- The forest resource is still harvested at an unsustainable rate which is not good for long term support by the industry to the Solomon Islands economy.
- Forestry will have to closely monitor every export log ponds to control exports.

5. Summary of past recommendations on logging sustainability

Past recommendations to improve logging sustainability are outline below and include: forestry regulatory measures; environmental measures; measures of export facilitation by Customs; immigration measures; and banking and exchange control measures.

Forestry Measures:

- Standards for Companies operating in the Forestry Industry must comply with under the Forest Resources and Timber Utilization Act (FRTUA) & Forest Regulations and Code of Logging Practices.
- SIG and provincial governments to consider methods to reduce harvesting levels to more sustainable levels:
- Limiting annual provincial harvesting levels.
- Introduction of a moratorium on the issue of new felling licences.
- Cancellation of existing licences for non-compliance or the breach of licence conditions. This may have the approach of issuing two yellow cards and third committal of forest offence will result in issuing of red card which indicates cancellation of felling Licences.
- Development of new, and enforcement of existing, ‘standard operating procedures’ for forest management practices by the Forestry Division e.g. no re-entry logging, conversion of degraded forests to plantations etc.
- Active enforcement of Act and Regulation (Protected Species, Levy and Mill Licensing, Fees, Felling Licences and procedures for issuance of felling licences, Licence conditions, Felling operations)

Environment Measures:

- The Director of Environment to diligently apply development control clauses of the Environment Act in particular the EIA process.
 - ECD will develop and implement a monitoring program in partnership with Ministry of Forestry and Research.
- To investigate all environmental damages as result of trespasses by logging companies.

- Develop specific guidelines for logging operations and incorporate them into the Environment Act and Regulations.
- Stop the issuing of licenses to non-commercial areas such as steep and high elevation areas and environmentally sensitive areas in commercial areas (already in SICOLP, Forestry Act/Bill).
- Enact a new legislation for the forestry sector which addresses the gaps of the current Forestry Resources and Timber Utilization Act and takes into account the present and projected timber and non-timber resource requirements of the country.

Customs Measures:

- More scrutiny over the Imports of logging machineries and equipment.
- More compliance regarding the exports of Solomon Round Logs
 - i. Customs is to apply a 100% physical check on all imports of logging machineries and equipment both by logging companies to ensure the right volume and value is declared.
 - ii. The joint log inspection task force comprising Forestry, Environment, Customs and Police is recommended to ensure the right volume and species is reported
 - iii. Customs review the number of sufferance ports around the country that were granted to logging companies.
 - iv. Establish a networking arrangement covering all stakeholders in this program to allow for a smooth flow of both intelligence and other relevant information.

Immigration Measures:

- Effective commencement of Human Smuggling and Trafficking regulations 2013, Harmonization and alignment of law enforcement agencies administrative processes and procedures, removal of Immigration legal breaching permit arrangements, effective joint operations and liaisons,
- Continuous joint Immigration Investigation & monitoring tours to the provinces, targeting logging camps, Honiara head offices and urban centres, effective enforcement of repatriation and removal instructions.

6. Logging Sustainability Policy: Key Recommendations

Recommendation 1) Ongoing Monitoring and Implementation

Cabinet to establish a cabinet-appointed committee to manage the ongoing monitoring of the banking facilitation issues and implementation of the Logging Sustainability Policy.

- To ensure the ongoing monitoring and reporting on these recommendations to Cabinet, a Cabinet-appointed Committee should be formed to progress the initiatives to put logging on a more sustainable path.
- The Cabinet-appointed Committee will also hold regular dialogue with SFA and the sawn timber representative body, SITPEA.
- The Committee will also continue close dialogue with the banking sector of facilitating export receipts.

Recommendation 2) Banking facilitation of logging receipts

The worst case scenario would cause a large shock to the Solomon Islands' economy and have a detrimental impact on growth and development of the country. While the Forestry Sector and the companies that operate in the sector will be directly affected, there will be wide-ranging impacts affecting landowners, employees – estimated to be around 10,000 skilled and unskilled employees – and businesses that sell to the Forestry Sector inputs to their activities and general consumption items.

The external sector may experience a Balance of Payments Crisis not witnessed since the global financial crisis in 2008, and it would likely be of a much larger magnitude. The Government's fiscal position will be put under strain given the large drop in domestic-sourced revenue and would place the Government in a Budget Deficit position.

Recommendations to improve banking facilitation, include:

- **Support POB in its attempts to improve its internal AML/CTF protocols** to allow the current prospective bank to set up an US dollar correspondent banking relationship with POB.
- **Continue regular consultation with POBs on discussions with the prospective bank** to enable quick reactions to any adverse decisions.

- **Commit to the Logging Sustainability Policy** (at page 23), which is aimed at putting the industry on a more sustainable footing and improving the integrity of the regulatory framework and the industry.
- **Officials to investigate further options with other foreign banks**, in the case where it looks unlikely that POB will be able to secure a US dollar corresponding bank in the short-term.

Recommendation 3) Reducing the volume of round logs being harvested and exported

Targeted reductions in the quantity exported.

Volume Exported Target	2019	2020	2021	2022	2023
	1,900,000m3	1,300,000m3	1,000,000m3	850,000m3	700,000m3

3.1 Minimum diameter of 50cm enforced

- A minimum diameter of 50cm is good for sustainability of the forest resources and ensures smaller/younger trees are not harvested. This will be policed by Forestry officials checking the loading at log ponds.

3.2 Monitoring and use of a quote system if needed

- While there will be a targeted reduction in the quantity of exports back to more sustainable levels, the enforcement of the minimum diameter will be the main mechanism to reduce the volume being exports.
- A secondary mechanism of a quota system may need to be implemented to achieve the targeted reductions, as well as specific restrictions of re-entry logging for a set amount of time, but these additional actions will only be enforce if the reductions cannot be achieve by the diameter enforcement.

3.3 Enforcement of LN114 – Only member of SFA will be able to fell and export round log (in the case of foreign investors). Restrictions will also apply to Indigenous companies, as they will be required to meet certain standards before allowed a license.

- Active enforcement of LN114 will help to ensure legitimate companies are operating in the forestry sector. In addition to SFA members, Indigenous companies can also apply for harvesting and export licenses, however, policing by Ministry of Forestry and investigation into whether indigenous people felling and export round logs are genuine businesses or a front for activity by foreigners will also be a focus of future work.
- A moratorium on any new logging companies (Foreign or Indigenous) could be enforced if needed.

3.4 Increase in the logging license from \$10,000 to \$50,000 per year

- The increase in the logging license is long overdue as it has not been increased for many years. Given that a license allows the export of 46,000 m3 per year, the increase to \$50,000 per year seems reasonable as it equates to around 0.1% of the average value of a m3.
- The increase in the logging license will also fund the decommissioning assessments and provide added resources for enhanced monitoring of logging activities.

Recommendation 4) Disincentivising the harvesting of small logs

4.1 There will be one export duty rate (a specific \$ amount) applied to all round log exports.

- The log prices are supposed to be set at the price it was sold for in the international market. It must be free from politics as that will obviously have detrimental impact on the fair sharing of benefit from logging.
- The Oceania Customs Organisation Secretariat (OCO) has recommend that Solomon Islands align its commodity classification with the Pacific Harmonized Commodity Description and Coding System.
- This would consolidate the current 80 subcategories to classify exported logs (species/grade) into a single code for the purposes of collecting export duty on round logs (HS code 4403).
- The proposed alignment would result in a move away from the current determined schedule where unique prices are determined for different species and grades, to a single price determined for all logs exported for export duty purposes.

- The proposed change would reduce the incentive for smaller/lower-value logs to be exported and for misclassification of logs to reduce export duty, as the same amount of export duty would be charged regardless of the value of the underlying log. This would likely have a positive impact on revenue.
- In 2016, around 25 per cent of exports were recorded as 'LOW GRADE'.
- The proposal will also disincentivise the export of low grade and small diameter species, and remove any opportunity for people to misclassify logs to pay less export duty.
- It may be appropriate to have two export duty prices used:
 - 1) One price to be applied to all round log species covered in the current Determined Value Schedule;
 - 2) A high price to cover the situation whether protected species are granted exemptions to be exported in round log form.

4.2 Base the export duty price on a transparent, reliable price reflective of Solomon Islands logs

- Currently, the Determined Value Schedule used to calculate the export duty chargeable on round logs exports, is based on data received via a price reporting database recording the price and quantity of Solomon Islands logs sold to other markets.
- Given a large majority of the logs are exported to China, the price and volume exported to the Chinese market heavily influences the Determined Value calculated for log species.
- However, the Chinese Government has recently stopped disclosure of all trade data to everyone. This is a likely reaction to the US and Chinese trade war to place tariffs on the others imports. As a result of the non-disclosure of data, there is a need to use an alternative, transparent, reliable price that is largely reflective of Solomon Islands logs.
- The monthly price of Malaysian hard wood logs are the prices that are largely reflective of the timber exported from Solomon Islands, and can be accessed monthly from the World Bank. The Malaysian log price is the world hard wood log price quoted by CBSI.
- **The current three-month average Malaysian log price is US\$276 per cubic meter, slightly above the Cost-Insurance-Freight value of Solomon Islands logs reported as going to China and Korea.**

Recommendation 5) Enforcement of current regulations and improved coordination between Government Ministries to ensure compliance by companies

5.1 All companies involved in harvesting and export of round logs will need to abide by a Code of Conduct and set procedures before logs are allowed to be shipped from the country

- It is important that all companies harvesting and exporting trees (SFA members and other indigenous companies) all meet certain minimum standards and can all be regulated.

5.2 Forestry officials to undertake 100 per cent checks for all log exports. Exports will not leave unless Forestry officials have completed checks

- 100 per cent checks by Forestry officials will ensure more oversight and checking of the exported cargo. Forestry officials present in the Provinces will also allow for the Code of Conduct to be more actively enforced. This recommendation will need funding via the Budget to pay for overtime for Forestry Officials required to work outside the normal work hours and to potentially establish accommodation closer to key log pond sites.
- The practice of applying for an export permit one day and the ship docking the next day will be stopped. Companies wanting to export logs will be encouraged to apply for export permits at least one week before loading, to allow time for Forestry officials to do the 100% and 10% checks on prepared cargo already in stacks ready for shipping. **Shipments cannot be loaded without a Forestry official present.** If shipments have not been cleared by Forestry, Customs will not let them leave.
- This recommendation requires a strategic plan of how to allow officials to be present when log shipments are being loaded. Currently, most of the shipments leaving Choisel are not checked by logging officials – this will also require resourcing by way of recruiting or transferring current employees from low activity logging areas.

5.3 Customs officials to undertake enhanced monitoring of forestry related imports. Customs to devote more resources to compliance and auditing of logging exports

- Revenue from logging activity accounts for around 60 per cent of total Customs collections and Customs performs a vital role in terms of trade facilitation — allowing exports to clear

and be transported to overseas markets.

- Customs will devote more resources to compliance and auditing of logging exports and ensure greater co-operation with the Ministry of Forestry in terms of allowing shipments to leave Solomon Islands.

5.4 All companies operating in Solomon Islands should pay income taxes on profits derived from economic activity in Solomon Islands

- It is core ta principle that tax should be paid in the jurisdiction where the economic activity that gave rise to the income occurs. In 2017, there were just under 2.7 million cubic meters of round logs exported from Solomon Islands. Taking the average log price over 2017, the total value of round log exports for 2017 was around SBD\$2.9 billion for 2017.
- Despite the value of logs being exported from Solomon Islands, there was little in comparison collected via income tax from companies involved in logging activities. While it is reasonable for logging companies to be in a loss position if large capital expenditures and other expenses create large tax deductions, the data shows that this is the case for many established companies. Inland Revenue needs to put additional resources into audit and assessment to ensure everyone pays the correct amount of income tax and economic value being derived in Solomon Islands is being taxed here.

5.5 Possibility of transfer pricing to be actively investigated

- The concern of base erosion and profit shifting is a concern that many countries have. Profit shifting via transfer pricing via non-arms' length is a way to move profits to other jurisdictions and avoid paying taxes. This is not only a concern for the forestry sector, but for other sectors and needs to be investigated.

5.6 Improved Co-ordination between ministries to ensure appropriate compliance against obligations before shipment leaves Solomon Islands

Recommendation 6) Incentivising environmentally friendly operations

6.1 Increase the logging bond from \$250,000 to \$1,000,000

- Administration of the current logging binds shows that the current bond is often inadequate for the costs of the environmental damage caused. Often companies will receive no bond returned and there are still high costs that are not covered by the bond. Increasing the bond to a level more reflective of the damage that could likely occur is environmentally responsible and can also act as a deterrent against bad environmental behaviour.

6.2 Environmental assessments post forestry activity.

- Environmental assessments to be conducted in combination with the Forestry Officer's Decommissioning assessment to check for environment impact from activity.

Recommendation 7) Supporting Downstream Processing

- Solomon Islands needs to progressively reduce its reliance on the revenue of log exports for economic, societal and environmental reasons.
- Processing a higher volume of logs domestically can be positive for the local economy – generates investment, creates jobs (both skilled and un-skilled), produces a higher value product than logs, ensures timber available for domestic use as local demand increases (through more permanent houses and large projects such as 2023 pacific games).
- The existing sawn timber industry, represented by SITPEA, is small relative to the logging industry. The entry of logging companies into timber processing will change the nature of the industry.
- SITPEA is a small organisation and does not have the capacity to manage large numbers of additional members. Restricting timber export approvals to SITPEA members would be a significant burden on the organisation and compromise its ability to manage its certification program. A better alternative is for SIG to continue to manage the timber export permit process as it currently does, and ensure there is sufficient resourcing for MOFR and other agencies to do this.
- SITPEA companies sell primarily to Australia and New Zealand, where there is strong demand for Solomon Islands timber if companies can comply with certification requirements. The entry of new companies that do not follow certification requirements would compromise these markets.

7.1 Ministry of Forestry's active enforcement of the 8 per cent requirement for round log licenses.

- The downstream processing ensures the country adds value to the portion of logs harvested. The current limit of 8% was reduced from the previous 20% of the felling Licence condition of the total volume of 50,000m³ allowed for export per licence from a concession area per annum. The implementation of the downstream processing requirement is weak and needs collective effort from Ministry of Forestry and the SFA to ensure improve compliance. After the condition of 8% of round logs for downstream processing was approved and applied, any company who do not comply is actually breaching the felling Licence condition and therefore

committing a forest offence.

- If logging companies cannot mill the 8 per cent, then it must be provided to the established sawmilling companies.

7.2 Strictly no exemptions provided to allow for the export of protected species in round log form.

- In recent times there have been exemptions provided to allow companies to export protected species in round log form. This is a direct contravention of the Act and directly undermines the sawn timber industry.
- The Ministry of Forestry has also received complaints about Solomon Islands sawn timber coming from Malaysia, which has likely been initially shipped there as a round log. This activity undermines the local downstream processing industry and their reputation in overseas markets.

7.3 Additional examination by an industry expert as to whether there should be a restriction that only SITPEA members can export sawn hard wood timber from Solomon Islands as a means of ensuring a quality Solomon Islands Timber product in the market. The SITPEA model (Audit – certification) is a robust framework (Independent and transparent) with an effective compliance mechanism (built within).

- During consultations with SITPEA, concerns were raised with companies entering the sawn timber industry and flooding overseas markets with low quality products to make short gains causing severe disruptions to long-term industry participants.
- While prohibiting the sawn hard wood timber export business opportunity to only SITPEA members (to date around 8 members) the intention would be to restrict market access, however, there would need to be an appropriate mechanism to all people to join SITPEA and not create a cartel type organisation.
- There needs to be further analysis of the industry by an industry expert to ascertain the best way to support downstream processing, while allowing for a competitive environment that encourage long-term participants that invest in the country and provide local employments to local citizens.

7.4 Continued collaboration between Ministry of Forestry and SITPEA

- There is currently a strong collaboration between the Ministry and SITPEA and it is important that the relationship continues to assist the sawn timber industry through initiatives such as improving sawn timber techniques, legal auditing of sawn timber products, access to markets, and utilisation training workshops.

7.5 A transparent and fair policy to be drafted on the eligibility and access to the transport subsidy for landowners to transport sawn timber to saw mills

Recommendation 8) Collaboration with key stakeholders

Increased collaboration with key stakeholders, includes:

- Increased collaboration between the Ministry of Forestry and Industry Associations;
- Increased Engagement with Provincial Government by the Cabinet-appointed Committee; and
- A communication strategy with provincial communities and traditional landowning groups.

Recommendation 9) Supporting alternative source of growth and livelihood projects in Provincial Areas

The economic activities in the rural areas was mostly driven by logging. Although some have depended very much on the commodity price of copra and cocoa. Relying on logging is obviously not sustainable, however history proves that in most part of the country, logging plays a critical roles in providing the avenues for locals to sale their produce in the market, short-term employees and other benefit related to downstream processing whereby some have access to decent houses.

Given the majority of the population are in the rural areas, the Government has to establish a dedicated working group to examine how to best support alternative sources of growth – such as tourism – to provide for livelihood opportunities as logging declines.

It is also vital that broader engagement and information sessions are conducted with Provincial Government and communication with landowners to develop a shared vision and understanding of the benefits of making logging more sustainable.

Recommendations include:

1. **Create a designated subcommittee/working group to focus on recommendations on how to best support alternative sources of growth.** This should include tourism as an avenue to provide for livelihood opportunities as logging declines.

2. **Government to prioritise policy effort and funding in the Budget to support identified alternative sources of growth, particularly Tourism.**
3. **Bolster efforts to combat transfer pricing as a mechanism to stop revenue leakage from alternative sources of growth, particularly the extractives industry.**
4. **Engagement with Provincial Government** by the Cabinet-appointed Committee to be created once Cabinet approves the Logging Sustainability Policy.
5. **Communication strategy** – to inform landowners and the broader population of the benefits of a more sustainable logging industry and the joint effort between the Government and SFA to provide a more sustainable future for Solomon Islands.

Recommendation 10) Improving the mapping and knowledge of Solomon Islands Forest resources and additional technical assistance

10.1 Ministry of Forestry to work with FAO to undertake a Forestry Inventory Assessment.

- Ministry of Forestry is in the process of assembling required information for FAO to conduct a Forestry Inventory Assessment.
- This is vital to get an updated view of the state of the commercial forest and to assess with a higher degree of confidence what the best medium term action may be to achieve sustainability.

10.2 The Forestry Industry Assessment to be used as the basis for further advice from Forestry experts on the current outlook for logging and possible new sustainable harvest options.

- Once the Forestry Inventory Assessment is completed, technical assistance should be sought to assess whether additional action is needed to place the forestry sector on a more sustainable path.
- Technical Assistance could be sought from Development Partner, such as FAO, or others such as the International Tropical Timber Association, which provides support under the UN Framework to the UN listed Least Developed Countries (LDCs), of which Solomon Islands is still member.

10.3 Improved mapping of forestry land area, by requiring land area is GPS traced before logging licenses are issued.

- Ministry of Forestry to formulate a GPS program and database to digitally trace the commercial forest and allow for an electronic database to track licenses issued.
- This could be enforced by requiring a condition of any new licenses to be that the land area is already GPS mapped for the Ministry of Forestry.
- Ministry of Forestry to seek assistance from development partners for this initiative.