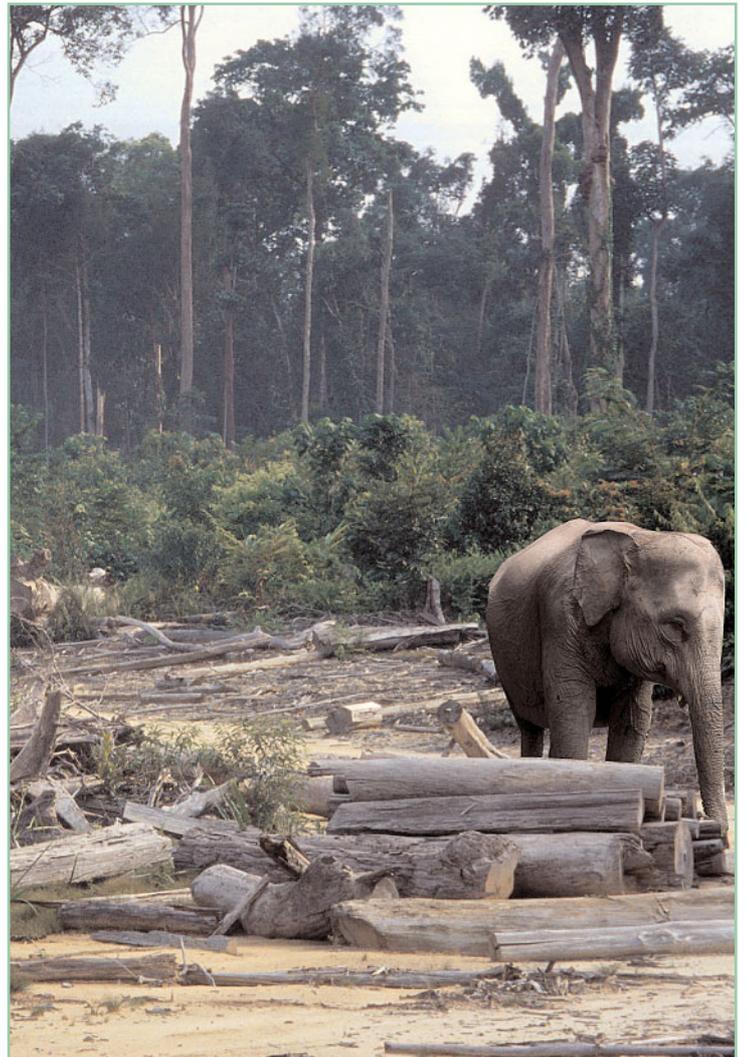




Elephant Forests on Sale

*Rain Forest loss in the Sumatran Tesso Nilo region and the
role of European banks and markets*

*A report commissioned by WWF Germany with support
from WWF US*



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First edition March 2003

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List of abbreviations:

APP	Asia Pulp & Paper Company Ltd.	HCVF	High Conservation Value Forest
APRIL	Asia Pacific Resources International Holdings Ltd.	HPH(k)	Hak Pengusahaan Hutan (kecil)
AREAS	Asian Rhino and Elephant Action Strategy	HTI	Hutan Tanaman Industri
BHK	Bleached Hardwood Kraft	IBRA	Indonesian Bank Restructuring Agency
CIFOR	Center for International Forestry Research	IKPP	Indah Kiat Pulp & Paper
CPO	Crude Palm Oil	IPK	Ijin Pemanfaatan Kayu
DBH	Diameter Breast Height	MoF	Ministry of Forestry
FFPCP	Forest Fire Prevention and Control Project	MTH	Mixed Tropical Hardwood
FoE	Friends of the Earth	NYSE	New York Stock Exchange
FWI	Forest Watch Indonesia	PKM	Palm Kernel Meal
GFW	Global Forest Watch	PKO	Palm Kernel Oil
JV	Joint Ventures	RAK	Riau Andalan Kertas
		RAPP	Riau Andalan Pulp & Paper
		RGM	Raja Garuda Mas Group
		SGS	Société Générale de Surveillance
		TNPA	Tesso Nilo Protected Area

Summary

This report focuses on the forces that threaten the Tesso Nilo forest in Riau province on the Indonesian island of Sumatra. Covering an area of almost 200,000 ha, the Tesso Nilo forest appears to be the largest remaining stretch of lowland tropical rainforest on the island. Covering half a million ha only two decades ago, today it stands like an island in an ocean of plantations. It has both extremely high plant diversity and extremely high levels of threat. This document has been prepared for WWF Germany by AIDEnvironment. It is based to a large extent on data provided by WWF's Asian Rhino and Elephant Action Strategy (AREAS) Riau Project which has worked on-site since 1999. The report presents the status of the Tesso Nilo forest as of the end of 2002, elaborates on the forces that threaten this forest and the landscape in which it resides. It explains how Riau-based wood and palm oil companies threaten the remaining forests and discusses the global markets that drive their activity. It concludes with strategies and recommendations that might be able to ensure the survival of this unique forest.

Forest loss on Sumatra

Between 1990 and 2002, Sumatra lost over 60% of its remaining lowland forest through conversion to settlements, oil palm and pulpwood plantations and other forms of agriculture. At this rate of deforestation, according to the World Bank, Sumatra is expected to lose its last lowland forests by 2005. Demand for timber of all types has put enormous pressure on Riau's forests. Demand for land for oil palm plantations has been very high, making Riau Indonesia's leading province for land area under this crop. As a result, more than 1,7 million hectares in this province alone had been deforested by the mid 1990s, 29% of Riau's original forest land. Especially its lowland and peat forests are heavily threatened by small and large-scale forest conversion.

Tesso Nilo's values and threats

The Tesso Nilo Forest Complex in Riau has one of the highest levels of plant diversity ever recorded by scientists anywhere on earth and supports populations of Sumatra's threatened elephants and tigers. Lack or absence of effective law enforcement, in part due to the chaotic decentralisation process started after the fall of president Suharto, is considered to be the major enabling factor.

Primary threats to the Tesso Nilo forest are:

- ▶ Industrial clear-cutting for pulpwood plantations to supply two giant pulp mills: RAPP and IKPP. In 2000, the two mills consumed half of Indonesia's or double (!) of Riau's legal wood supply and accounted for around 60% of Indonesia's total pulp production. The mills have to operate at capacity to pay back the huge debt their construction cost, but they cannot operate at capacity with the timber legally available from natural forests clearings and plantations. This discrepancy has become a major driving force behind the illegal logging in the province of Riau.
- ▶ Industrial and community-based legal and illegal forest clearance for oil palm plantations to supply palm oil mills with local, regional, national and international customers: Wood from the clearings supplies pulp, plywood and saw mills.
- ▶ Legal and illegal logging for local, regional, national and international use: The province has a concentration of wood-based industries, including plywood mills, moulding factories and hundreds of legal and illegal sawmills. Some 80% of the Tesso Nilo forest continues to be managed by four logging companies. Illegal logging is very common in Tesso Nilo.

Secondary threats are:

- ▶ Encroachment after forests are opened by construction of roads and corridors to facilitate log extraction.
- ▶ Poaching of wildlife after access to the forest is eased by new roads and

more and more people enter the forest to extract timber.

- ▶ Fires used for clearing that jump containment lines and damage surrounding forests.

International trade links

Indonesia's logging and plantation industries produce timber, pulp, paper and palm oil for the rapidly expanding global market. Europe is a major customer. Riau ranks third among 27 provinces, supplying 12.5% of the country's non-oil & gas export value, mostly based on industries that depend on forest conversion.

Over 50% of the stationary paper wholesale supply business in the United Kingdom may contain Indonesian paper from Asia Pulp and Paper Ltd. (APP), quite possibly coming from its plant near Tesso Nilo. Among European countries importing Indonesian pulp, Germany ranks 5th. The web site of the National Agency for Export Development lists four Dutch companies as importers of Indonesian paper, one of them is a world leader in graphic board.

Two years ago, the Finnish paper giant UPM-Kymmene bought Asia Pacific Resources International Holdings Ltd. (APRIL) share of a large paper mill in China and became the sole owner. APRIL is a Singapur-based Holding company which owns also the pulp giant RAPP that is active in Riau Province. This was followed by an agreement between the two companies that made UPM-Kymmene the biggest customer of RAPP. The companies also have financial ties, a UPM-Kymmene granted APRIL a US\$ 121 million loan in 1999.

Foreign financial institutions have financed to a large extent the strong expansion of pulp & paper and oil palm companies operating in Tesso Nilo and the surrounding forests in the province of Riau, by helping them to issue shares and bonds, by buying their shares and bonds, by providing loans, and by extending credit guarantees. Especially with respect to the financing of the giant IKPP pulp mill in Perawang, a large

number of German financial institutions played a significant role. IKPP is the most important Indonesian subsidiary of the Singaporean company Asia Pulp & Paper (APP), which has been engaged in complicated negotiations on the restructuring of its giant US\$ 13.4 billion debt since March 2001. Three German financial institutions, Deutsche Bank, HypoVereinsbank and Hermes Kreditversicherung, are actively involved in these debt restructuring talks. The debt restructuring negotiations center on determining the cash flow IKPP can generate and how much of that cash should be repaid to the creditors. IKPP generates a lot of its cash by pulping mixed tropical hardwood forests. The negotiations of the creditors therefore directly influence the survival of Riau's remaining natural forests. They would have the ability to tie strong environmental protection terms to any agreement they sign.

A conservation framework for Tesso Nilo

Tesso Nilo is strategically located between four existing reserves, together they would form an ecological network of 600,000 ha of protected forest. In the 1980s and again in the 1990s, Tesso Nilo had been proposed as a protected area. The proposals were rejected after heavy lobbying by the timber industry, because Tesso's flat lowland forest was easy to harvest and too valuable to leave standing. In April 2001, WWF proposed to the Ministry of Forestry to declare 153,000 ha of Tesso Nilo an elephant conservation area. The proposal received wide local political support and has been accepted by local communities and various commercial stakeholders. At the time of writing in March 2003, the final decision by the Minister of Forestry was still pending.

However, official protection status for Tesso Nilo would only be a very first step. Subsequently, the forest would need to be secured by stopping rampant tiger poaching and illegal logging and by stabilising the conversion frontier. The largely industrial land use

practices in adjacent lands would need to be made more compatible with conservation needs, such as allowing wildlife movements and protecting water supplies and watershed functions. WWF-AREAS Riau's ultimate vision is a three million ha multiple-use conservation landscape that includes five protected areas.

While a certain momentum for the protection of Tesso Nilo started building up in the past two years, threats to the forest remain strong, however. Dozens of illegal sawmills receive endless truck loads of illegally cut timber every day, tiger poaching is rampant, and communities are converting small forest patches into oil palm plantations. Threats to the wider Tesso Nilo landscape and the whole province of Riau are even more severe. Each of the two pulp and paper conglomerates operating in Riau plans to clear at least another 200,000 ha of forest, most of it likely in the fragile peat swamps.

WWF's campaign work

WWF calls on these main players to work together to save Tesso Nilo and other High Conservation Value Forests:

- **The Indonesian Government** should declare the whole Tesso Nilo forest as a protected area and ensure that it is effectively managed. The Government of Indonesia should help create wildlife corridors to link Tesso Nilo to other existing protected areas and ensure their full protection. GoI should develop, communicate, and enforce a clear policy that protects all High Conservation Value Forests (HCVF). WWF is prepared to help develop that policy and provide tools for the identification of High Conservation Value Forests.

- **Riau's provincial and district governments** should review land-use plans to prevent further conversion of High Conservation Value Forests and ensure that the province's natural resources are developed sustainably. WWF is prepared to help develop new or re-design existing land use plans in

partnership with government authorities and other stakeholders.

- **Riau's pulp and paper industry** should protect the High Conservation Value Forests within their concessions and those of all their suppliers, operate within the limits of clearly defined legal and environmentally and socially sustainable wood supply plans, and ensure sound forest stewardship in plantations from which they source fibre for paper.

- **Financial Institutions and Banks who invest in the pulp and paper industry in this region** should ensure that their investments are not being used to support the conversion of HCVF or the violation of traditional land rights.

- **Customers** of products from this region should ask for environmentally sustainable manufacturing processes so their purchases do not lead to the destruction of more natural forest and the deaths of elephants and other wildlife.

Recommendations by this study

The following recommendations by AIDEnvironment are complementary to the numerous actions and initiatives that WWF, other NGOs and parts of the private sector have taken already to save Tesso Nilo and other forests in Riau. Some of the recommendations below are already implemented or currently being discussed by the NGOs active in Riau; in that case, their mentioning here is meant as encouragement.

It has become clear that the next few years will be critical in preventing complete deforestation of the Tesso Nilo Forest and other natural forest blocks remaining in the Tesso Nilo Conservation Landscape. Land use decisions in the province are influenced by a complex web of public and private entities operating at local, provincial, national and international levels.

The fundamental recommendation of this study is that, in view of the urgency of the situation in Tesso Nilo, it is essential that the multi-stakeholder process involving the private sector,

government and NGOs gains force and momentum. Vigorous campaigning by NGOs and by consumers of products that may have been produced in the Tesso Nilo region must maintain the necessary pressure.

Recommendations directed at the government sector refer to:

- Creation of enabling policy environments for sustainable land use, industry and trade, by the Indonesian government and by governments of consumer countries.
- Effective implementation of a new, sound land use plan for Riau.
- Establish a trust fund to ensure longterm financial sustainability of managing and protecting the Tesso Nilo protected area.
- ‘Good governance’ donor programs that help strengthen provincial and local government institutions.
- Enact legislation, both in Indonesia and in countries importing goods from tropical forest lands, on transparency requirements for business corporations.
- Help establish an independent monitoring / watchdog structure.

To the private sector:

- Logging concessionaires should adopt certain conservation principles.
- Willingness to agree on fair take-overs of concessions with high biodiversity values by a conservation organisation.
- Develop and apply best practices for their sector, and apply transparency rules in their entire production or investment chain.
- Corporations in the supply chain for timber, pulp & paper and palm oil should join WWF’s efforts to evaluate the conservation value of the forests which would be converted, and ask their suppliers to respect the evaluation and to not convert high conservation value forests. A temporary moratorium on forest conversion should be put into place until all forests have been evaluated.

To the financial sector:

- Loans granted by investors, financial institutions and export credit agencies should be based on strict environmental and social criteria and related monitoring mechanisms.
- Facilitate investments and contributions to a sustainable development trust fund that supports alternative livelihood options for local communities.
- Improved due diligence practices for funding projects in the sectors of agriculture and forests.

Acknowledgements

The author gratefully acknowledges the valuable support received from his colleagues Lilian Spijkerman, Eric Wakker and Wolfgang Richert. Jan Willem van Gelder (Profundo) provided vital inputs in the financial sections. Michael Stuewe (WWF-US AREAS) provided essential backstopping and feedback to drafts of the report. Patrick Anderson (AREAS Riau), Nazir Foead (WWF Indonesia), and Christine Wulandari (WWF Indonesia) provided welcome feedback and inputs. Ed Matthew (FoE) and Chris Barr (CIFOR) generously made recent statistics available. Finally, AIDEnvironment thanks Alois Vedder, Martin Geiger, Bernhard Bauske and Markus Radday of WWF Germany for commissioning this paper and for their valuable support.

Large sections of this study are based on reports, data, maps and opportunistic information compiled by Nazir Foead, Purwo Susanto, Bambang Hartono and their team at WWF Indonesia's Asian Rhino and Elephant Action Strategy (AREAS) Riau Project. AREAS Riau had identified the Tesso Nilo Forest as essential habitat for the Sumatran elephant and tiger and as an absolutely outstanding forest on the global biodiversity scale. The AREAS Riau project has been supported by the AREAS Technical Support Network's Steve Osofsky (WWF US), Michael Stuewe (WWF US), Ajay Desai and Martin Hardiono, and several professionals from the WWF Network, among them Agus Purnomo and Agus Satiaso (WWF Indonesia), Jennifer Biringer, Jim Fuschetti, Francis Grant-Suttie, and Eugene Lee (all WWF US), Tom Vellacott (WWF CH), M. Eishi (WWF Japan), Christy Williams and Rod Taylor (WWF International).

For more information on AREAS, please check www.worldwildlife.org/area.

1. Introduction

This study brought together and synthesised the findings and insights obtained in recent years by the WWF-AREAS project, by the Centre for International Forestry Research (CIFOR, Barr and Potter & Badcock) and by Forest Watch Indonesia / Global Forest Watch. Apart from this, the study examined trade links between Tesso Nilo and the European market.

What is at stake

The Tesso Nilo Forest Complex in the Indonesian province of Riau (see Figure 1), is one of the last and largest remaining tracts of lowland rainforest in Sumatra. The forest has one of the highest levels of plant diversity ever recorded by scientists anywhere on earth and supports populations of Sumatra's threatened elephants and tigers. The Tesso Nilo complex, especially its lowland and peat forests, has come under heavy pressure from rapidly advancing, largely industry-driven deforestation and forest degradation. In many other parts of Sumatra, and Riau in particular, large areas of natural forest have been clear-cut and planted with hundreds of thousands of oil palms and fast-growing trees for the pulp and paper mills. Until recently, that appeared to be Tesso Nilo's future as well. Since 1985, the forest has lost over 300,000 ha to the oil palm and pulp and paper industry, only about 190,000 ha remain today.

Legal and illegal logging and plantation industries in this part of Riau produce timber, paper and palm oil for the rapidly expanding global market. Europe is one of the biggest consumers. In the Netherlands, Siak Raya plywood and APRIL's PaperOne copying paper are sold. In the UK people write on APP paper. In Italy, use tissues are made from Riau pulp. Supermarkets sell a variety of products that are likely to contain palm oil from the plantations of PT Inti Indosawit Subur or the Sinar Mas Group. The various companies involved in the process of forest destruction hold financial relations with European banks and other financial institutions.

In short, there is a web of international market actors behind the companies threatening Tesso Nilo, many of whom are not aware of the fact that their activities play a role in the destruction of one of Indonesia's biodiversity hotspots. If current patterns continue, Tesso Nilo's natural treasures will be lost within the next few years. Saving Tesso Nilo therefore requires changes in international trade and production policies and consumption patterns.

WWF's goals

In February 1999, WWF's Asian Rhino and Elephant Action Strategy (AREAS) project¹ began establishing a "safe haven" for one of the largest remaining populations of the Sumatran elephant in Riau, Sumatra. The island's elephant population has come under increasing threat by rapid forest conversion. As forests are lost, elephants feed in fields and plantations, generating conflict with humans that often results in the death of the elephants by poisoning or captures. Elephants need large forests to feed in and they need adjacent land uses that do not attract them into fields and plantations where they might get killed by angry farmers. AREAS found the Tesso Nilo Lowland Forest to be the largest remaining block of ideal Sumatran elephant habitat. Fortunately, the remaining forest was surrounded to a large extent by a land use type -acacia pulp plantations- that was unlikely to

attract elephants, and thus would not create major human-elephant conflicts. The AREAS project therefore suggested to protect the Tesso Nilo forest from conversion to plantations, phase out the on-going logging operations, and create a protected area. The new reserve would have a strategic location between Kerumutan Wildlife Reserve, Bukit Rimbang Bukit Baling Wildlife Reserve, Bukit Bungkuk Reserve, and Bukit Tigapuluh National Park (see figure 1). The establishment of a Tesso Nilo Protected Area (TNPA) and the protection and rehabilitation of forested wildlife corridors connecting some of the reserves would create a 600,000 ha protected ecological network within a 3 million ha conservation landscape.

Achieving official protection status for Tesso Nilo would only be a very first step. Subsequently, the protected forests in the whole conservation landscape would need to be maintained and secured by stabilising the conversion frontier, and by making both industrial and community land use practices in adjacent lands more compatible with the conservation needs of the forests.

Since 2001, WWF has been working on these two fronts: establishing a protected area and promoting changes to land use practices in the adjacent lands. In 2002, the momentum towards a viable conservation scenario for the whole landscape began building up when the Critical Ecosystems Partnership Fund

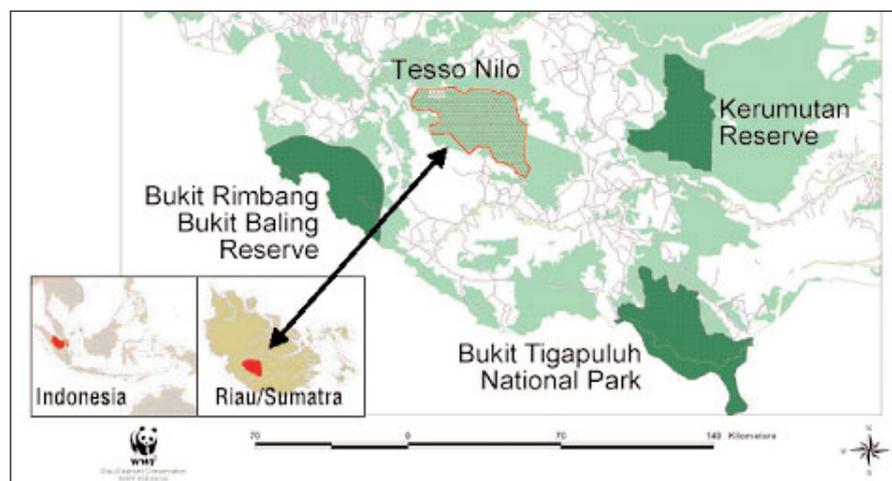


Figure 1. Location of the Tesso Nilo Forest and three of four existing reserves; their position within Riau and Indonesia (WWF-AREAS Riau, Martin Hardiono).

declared it an investment hotspot, and 24 local non-governmental organizations joined in an alliance to protect the now called Tesso Nilo – Bukit Tigapuluh Conservation landscape.

Momentum for change

In 1984 and in 1992, Tesso Nilo has been proposed as a protected area. Each time, the proposal was rejected after heavy lobbying by the timber industry. In the latest attempt, in April 2001, the Ministry of Forestry's Department of Conservation and WWF proposed 153,000 ha of Tesso Nilo to be declared an elephant conservation area. The final decision by the Minister was still pending in March 2003.

Two international pulp and paper conglomerates operate pulpwood plantations adjacent to Tesso Nilo. After negotiations with WWF these companies declared that they will not convert any more Tesso Nilo forest, stop purchasing wood illegally cut in the forest, and

support the declaration of a Tesso Nilo Protected Area. If the companies take these commitments seriously, it would mean a great step forward in reducing the pressure on Tesso Nilo. Four logging companies hold licenses to log inside Tesso Nilo. The government-owned company Inhutani IV has agreed to hand over its concession to a new protected area. The three private companies have agreed, in principle, to work with the Indonesian Government and WWF to select areas of their concessions inside Tesso Nilo to be put off limits to logging. Several local communities which have been heavily involved in illegal logging, have indicated their willingness to give up land claims in case Tesso Nilo would be declared a protected area, to refrain from illegal logging and to assist in preventing illegal logging by outsiders. In return, they expect government to stop all illegal logging in the forest, and WWF to support them in sustainable development

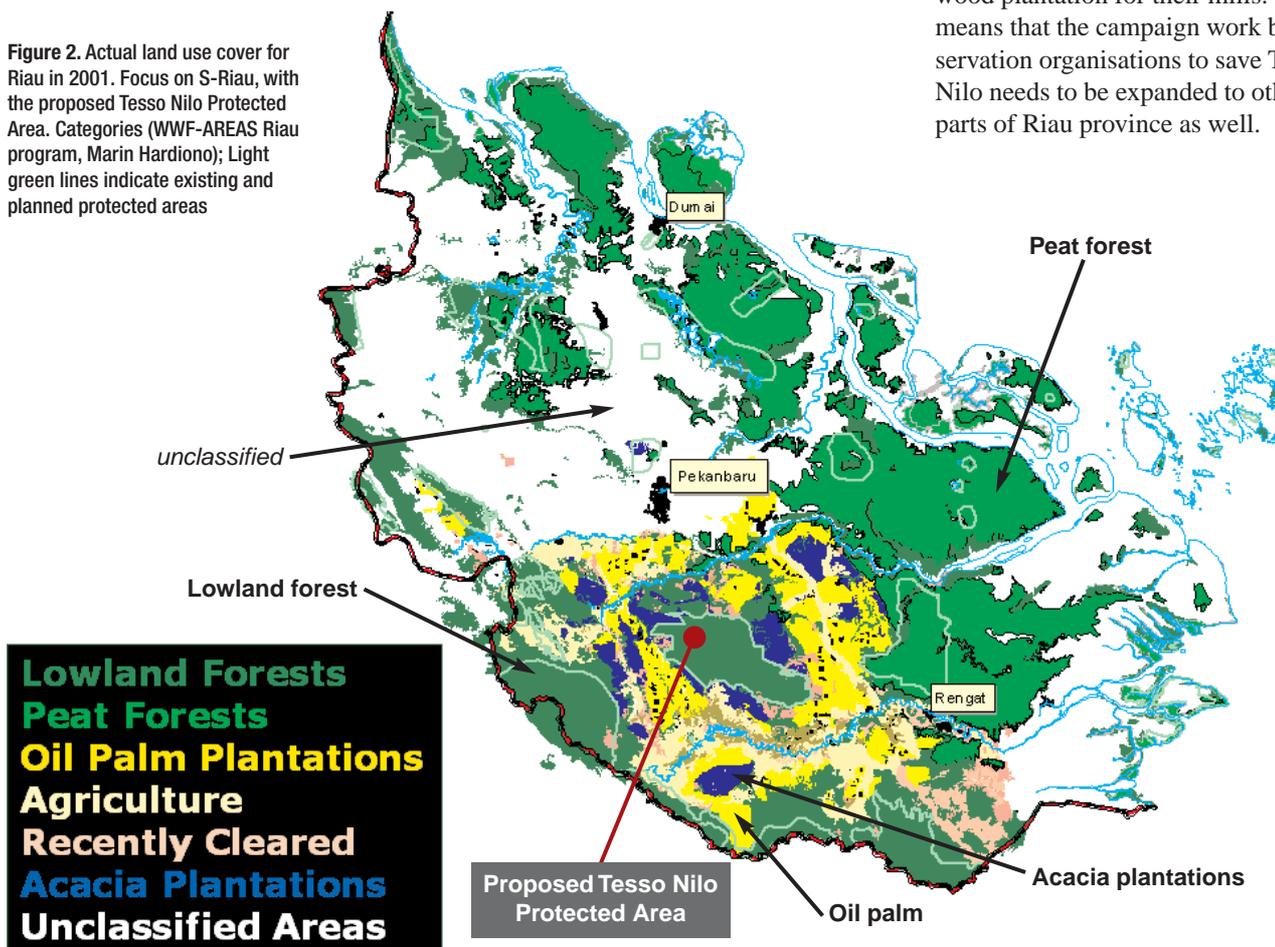
projects. They are inspired by the experiences of several community representatives in other protected areas in Sumatra and Java during recent visits organised by WWF.

The need to remain alert

Threats to the Tesso Nilo forest remain, however. There are dozens of illegal sawmills that receive illegally cut wood from Tesso Nilo. There appear to be high levels of tiger poaching, likely facilitated by the density of illegal loggers in the forest. There is constant uncertainty about the possible expansion of community oil palm plantations into protected forest. And in the fragile Indonesian political climate there is always the possibility that the pulp and paper companies are able to use their power to influence political decision makers to overturn agreements and open the forest for conversion after all.

Each of the two mother companies of the pulp & paper mills operating in Tesso Nilo still plans to convert at least another 200,000 ha of forest to pulpwood plantation for their mills. This means that the campaign work by conservation organisations to save Tesso Nilo needs to be expanded to other parts of Riau province as well.

Figure 2. Actual land use cover for Riau in 2001. Focus on S-Riau, with the proposed Tesso Nilo Protected Area. Categories (WWF-AREAS Riau program, Marin Hardiono); Light green lines indicate existing and planned protected areas



2. Profile of the Tesso Nilo forest

Location and description

The Tesso Nilo Forest covers an area of 188,000 ha and is located in the Pelalawan, Kuantan Singingi, Kampar and Indragiri Hulu Districts, in the province of Riau in the central part of the Indonesian island Sumatra (ca. 102°E and equator). Acacia plantations surround about ca. 80% of the Tesso Nilo Forest, 15% is surrounded by oil palm estates and 5% of the forest borders village gardens. About 1.5 hours drive north of the Tesso Nilo forest lies Pekanbaru, the capital of the Sumatran province of Riau that has the character of a “gold rush” town built by timber and oil barons. Riau is one of the richest provinces in Indonesia, yet more than 40% of the population lives below the poverty line.

The Tesso Nilo Forest Complex harbours humid tropical lowland forests and some peat swamp forests and its altitude ranges from 25 to 500 meters above sea level. With annual rainfalls of 2000–3000 mm, this lowland tropical rainforest classifies as super humid. During the occurrence of the El Niño phenomenon, however, many trees may be defoliated and some eventually die off. Episodic droughts of this kind facilitate forest removal by human-induced fire, as has been the case in recent years.

Biodiversity and flagship species

A recent survey commissioned by WWF in the Tesso Nilo forest found up to 218 vascular plant species in single 200 square metre plots. This equals one different vascular plant species on every square meter, a much higher diversity than the authors found in over 1800 similar plots studied with the same technique in tropical lowland rainforests in 19 other countries, including Brazil, Cameroon, New Guinea, and Peru. In short, Tesso Nilo appears to be one of the most diverse forests on earth.²

Tesso Nilo is also home to a wide range of large wildlife including Sumatran elephant (*Elephas maximus sumatrensis*), Sumatran tiger (*Panthera tigris sumatrae*), gibbons (*Hylobates* spp.), tapir (*Tapirus indicus*) and several threatened bird and reptile species.

According to the Ministry of Forestry’s executing conservation department at the provincial level, up to 170 of the few hundred elephants that may still survive in the province may live in the forests of Tesso Nilo.

Another flagship species on the verge of becoming extinct but still present in the Tesso Nilo forest is the Sumatran tiger. Around 1900 there were three subspecies of the tiger (*Panthera tigris*) in Indonesia. Today, both the Bali and Java tiger have become extinct and only the Sumatran subspecies survives.

Prior to 1950, the tiger was more or less continuously distributed throughout the entire island of Sumatra. Now, as a result of the conversion of natural forest to agricultural holdings and poaching, the tiger distribution has become fragmented and substantially reduced. Tigers in Sumatra can maintain a density of 1 per 100 km² in mountainous areas and 1–3 per 100 km² in more favourable lowland habitats.⁴ At present, estimates of tiger densities in the forests of Tesso Nilo are not known. Sadly, the apparently high density of

Human-Elephant conflict

Asian elephants may face extinction on the island of Sumatra if the mixture of grassland and forest which is their preferred habitat continues to be destroyed. The remaining population in Sumatra is almost impossible to determine, some guess that it may be about 3000 individuals. As forests become fragmented, elephants no longer find enough food and start feeding in village gardens and oil palm plantations that replaced the forest. This causes conflicts with the new land owners who try to keep elephants out of their fields. If unsuccessful, they either poison the crop raiders or call in capture teams from the Ministry of Forestry’s executing conservation department to remove them. The latter have not been very successful in keeping captured elephants alive. A dramatic decline of the elephant population is the result. Experts consider such human-elephant conflicts to be the leading cause of elephant deaths throughout their Asian range states. The situation is particularly pressing in Riau. The province holds a large percentage of Sumatra’s total elephant population, but also harbours Indonesia’s largest area under oil palm. As human populations increase and more and more forest is converted to estates and agricultural lands, elephant-human conflicts are on the rise. Riau’s elephants are increasingly forced to raid plantations and village gardens that surround the forests,

in search of food and safety. They are constantly chased by angry farmers and in grave danger of being poisoned or shot by the farmers. In one dramatic case in Riau in 1996, an oil palm company poisoned 12 elephants at once. In another on the border of Riau and North-Sumatra, a community poisoned 17 elephants who all died within just 200 meters of each other. Single elephant deaths by poisoning are regularly reported. Still more elephants, however, are captured and put into a so-called Elephant Training Centers by government teams with poor training and equipment. Most of these captured elephants eventually succumb to their capture trauma or subsequent poor holding conditions. Direct damage caused by elephants (trampling of houses, injuring and killing people and damage to small and large scale plantations) in and around Tesso Nilo is estimated at 4.5 million US\$ over the period 1997–2000.³ During the past four years, at least 10 people were killed and 6 others wounded in attacks by wild elephants in areas adjoining the South Bukit Barisan National Park in southern Sumatra.

Sources : WWF Endangered Species Programme (www.panda.org/species, then follow ‘Asian Elephants’); *Forests, People and Rights, Down to Earth Special Report: June 2002*; *Jakarta Post*, 14 Feb.2002; WWF Indonesia, 2001.

tigers in Tesso Nilo so far has only been confirmed by the frequency of attacks on illegal loggers and evidence of poaching incidents. At least 33 tigers were poached in the last four years in the Tesso Nilo Landscape. The main threat to the tiger population in Tesso Nilo appears to be poaching.⁵ The many legal and illegal loggers in the forest are likely to find and report tiger signs to potential poachers, and their numbers make it difficult for authorities to identify the actual poacher.

The tiger, the elephant, and some of the world's richest forests are with their backs against the wall in Sumatra. Prospects for the long-term survival of both forest and wildlife appear to be grim if natural forests continue to be converted to monocultures. But even the existing protected areas are under threat from illegal logging and tiger poaching. Only an effectively managed

ecological network of protected areas and corridors and anti-poaching measures would allow far-ranging wildlife such as elephants and tigers to disperse and form viable populations.

Deforestation and forest status

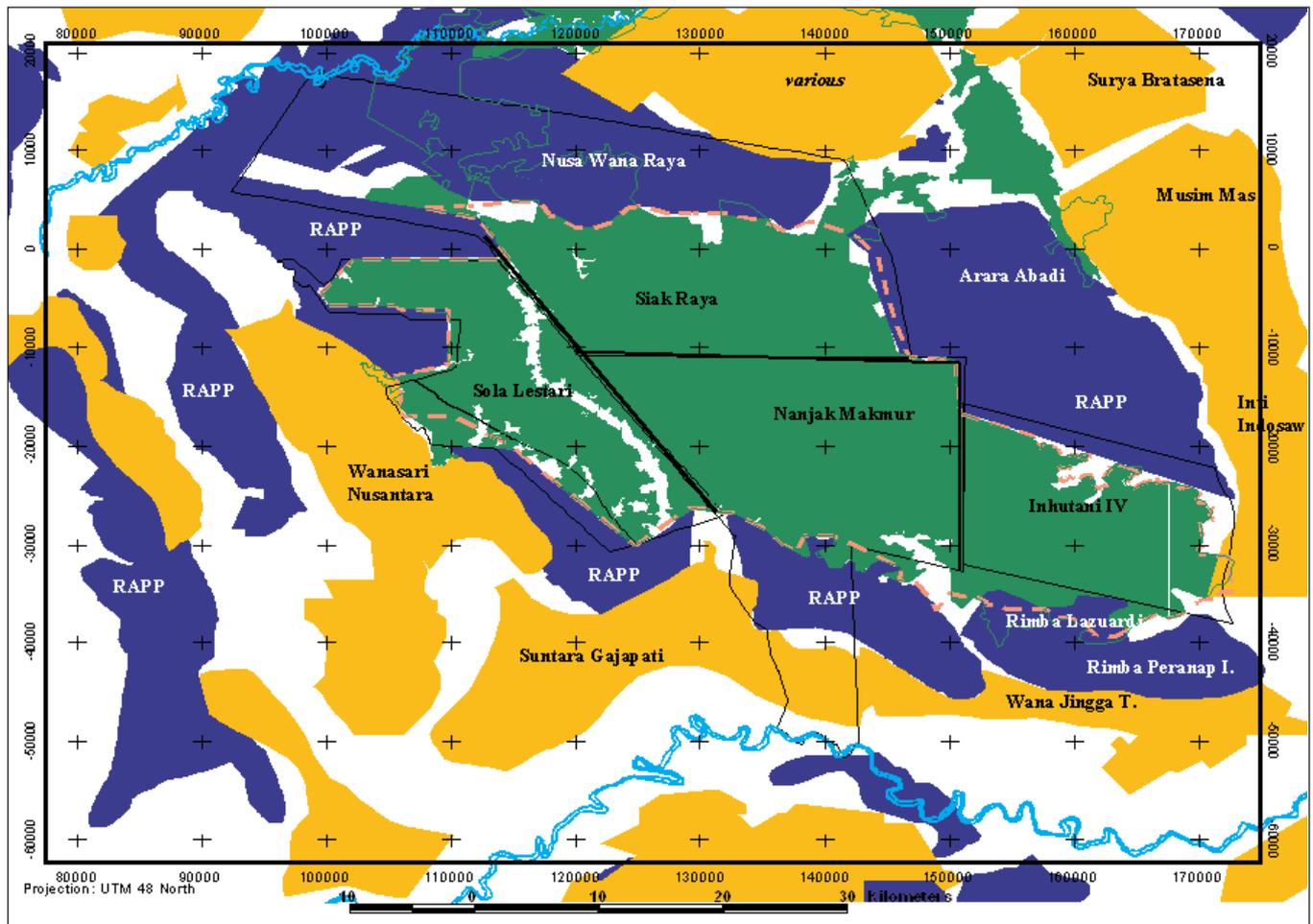
Fifty years ago, millions of hectares of tropical rainforest covered the length of the Sumatran island. Over the last 12 years more than 60% of the remaining Sumatran lowland forest was lost through logging, conversion to settlements, oil palm and pulpwood plantations and other forms of agriculture.⁶ With the current rate of deforestation, Sumatra is expected to lose the last remaining tracts of lowland forest by 2005, leaving clear-cut wastelands and pulp wood and palm oil plantations virtually devoid of forest species.⁷

By the mid-1990s, more than 1,7 million hectares in Riau alone had been

deforested, 29% of Riau's original forest land. Riau has been particularly affected by deforestation, the overall percentage for Sumatra is "only" 17%.⁸ Based on studies carried out by the WWF-AREAS project, conservative estimates indicate that from 1999 onwards the Tesso Nilo forest has been disappearing at a rate of 56 ha per day.

The 188,000 ha of natural forest remaining in the Tesso Nilo Forest Complex may be divided into three sections. Tesso Nilo West consists of about 33,000 ha with conversion forest status leased by several companies. This forest is slated to be converted to plantations. Tesso Nilo Central covers about 120,000 ha, with a "limited production" forest status and has been leased to three companies for selective logging (PT Siak Raya, PT Hutani Sola Lestari en PT Nanjak Makmur). Tesso Nilo East has about 35,000 ha of "limited produc-

Figure 3. Concessions and plantations in and around the Tesso Nilo Forest (WWF-AREAS, Martin Hardiono): Blue - acacia plantations, green - lowland forest, yellow - oil palm plantations.



tion” forest status leased by the government company Inhutani IV for rehabilitation and/or logging (see figure 3).

Poorly controlled logging practices in the proposed conservation area have resulted in widespread damage to standing vegetation, changes in local hydrology and extensive in-filling of streams. The statutory 500m limit to clear-felling on either side of the main road network in the RAPP plantation concession has been exceeded in many cases. Moreover, roads are providing easy access to illegal loggers and poachers.⁹

the current concession rights expire in another 17 years. Another 33,000 ha of forest has been designated for conversion to plantations (Hutan Tanaman Industri: HTI).

Conservation history

The Tesso Nilo forest was first proposed as elephant reserve in 1984. The forest area was 496,000 ha at that time. The Ministry of Forestry rejected the proposal after intensive lobbying by the local logging industry. In 1992, the area was proposed again, the remaining forest area at this time was 300,000 ha. Again, the Ministry of Forestry rejected it because of lobbying by the logging and plantation industries. In April 2001, WWF proposed 153,000 ha of the remaining 188,000 ha to be declared an elephant conservation area, and again the local industries responded by initiating an intensive lobbying campaign. The decision on WWF’s latest proposal to protect the Tesso Nilo Forest Complex is still pending. However, there are rumours that the Government may soon announce the protection of the first phase of Tesso Nilo: the 33,000 ha Tesso Nilo East which the Government controls through a state company.

The 2000 forestry reform stated that existing logging concessions would gradually be phased out and no new logging permits would be issued as of January 2001. In 2000, the leases of the logging concessions in Tesso Nilo had expired and the majority of local districts and villages supported the conservation proposal. However, just before the deadline, the licenses were renewed for another 20 years. Today, 155,000 ha have been designated for selective logging (Hak Pengusahaan Hutan: HPH) in Tesso Nilo Central and East. If no rezoning happens, the forest could only obtain a legally protected status after

3. Major threats

3.1 General overview

Some of Riau's forests have been exploited for many decades and over a century. But since the 1970s, vast stretches of Riau's original land cover have been exposed to three or four major exploitation cycles. First, very high value tree species were selectively cut for export as round logs. Next, more saturating cutting of species with lower value for furniture, plywood and round log export began. Then over-logged so-called wastelands were cleared to supply pulp mills. And finally, either acacia or palm oil plantations were established on many of the clear-cut areas.¹⁰

The area surrounding the Tesso Nilo Forest complex is in the third or fourth cycle, having either plantations or clearcut areas that are not being replanted because of land disputes. Tesso Nilo itself is in the first or second cycle, with legal, selective logging operations feeding the provincial sawmill industry. However, illegal loggers and small and large-scale forest conversions continue to threaten the remaining natural forest.

The shift from logging natural forest to irreversible forest conversion in the region is the result of relatively simple market dynamics. A logging company may now find it difficult to attract financial institutions that are willing to finance long-term forest management programs which have to compete with short-term plantation alternatives: if the logged natural forest is converted into palm oil plantations positive cash flows can be achieved three years after planting and profits may be expected after seven years. Similarly, conversion of natural forest into rapidly growing softwood plantations can generate positive cash flow within seven years. Annual crops, such as soybean, could provide even quicker incomes.

In summary, exploitation of Tesso Nilo is driven by four overriding motives:

- Legal logging for the timber (sawnwood and plywood) industry.
- Illegal logging for local and out-of-state illegal and commercial sawmills and export to Singapore and Malaysia.

- Industrial clear-cutting of natural forests to establish pulpwood (mostly acacia) or oil palm plantations.

- Small-scale clear-cutting to generate wood for the pulp industry and to establish community oil palm plantations.

Questionable legal and obviously illegal operations are facilitated by four overriding factors:

- Poor "interpretation" of laws and regulations when licenses are issued.

- Construction of roads and corridors to facilitate legal log extraction.

- Poor enforcement of laws and regulations.

- Willingness of the legal industry to accept illegally harvested timber.

Underlying factors that drive these threats are:

- Poorly functioning government institutions (lack of staff and resources, uncertainty about mandates, widespread corruption).

- Absence of planning and consultation with all relevant stakeholders.

- Severe overcapacity of wood-processing industries in relation to what can be supplied from sustainable timber and pulpwood sources in the region.

- Huge corporate debts, incurred by unsustainable company growth and siphoning off of profits and loans by managing families, which force companies to operate at maximum capacity.

- A rather chaotic decentralisation process which has led to responsibility conflicts between national and lower-level governments.

- Indonesia's and the region's general financial and economic crisis.

- Uncontrolled markets, in the sense of inadequate social and environmental regulations regarding the sources of raw materials harvested from forests or from converted forest lands, and -if regulations and legislation do exist- their poor enforcement.

The wider Tesso Nilo area represents a clear case of the usual cycle of conglomerate-driven forest destruction in Indonesia: first, a company associated with one of the conglomerates applies and receives a permit to selectively log

an area. The harvested logs go to a conglomerate-owned sawmill. Although Indonesia's forest law allows selective logging under a system that would leave the forest 35 years to recover, companies seem to over-log the area deliberately. Next, an application is submitted to the government to have the over-logged area declared "degraded", which implies that the area is no longer fit to be called a forest and should be converted to a plantation. This change in status requires an official reclassification of the forest land.

Once that change of status is approved, another company – often a sister belonging to the same conglomerate – applies for a license to convert that new "wasteland" forest to either oil palm or acacia pulp wood plantation. Whichever plantation it will be, the remaining trees are removed and go to a pulp mill. Then either oil palm or acacia plantations are established, the products of which go to the respective mills, likely to be members of the same conglomerate. Indonesian law regulates the size of concession areas any given parent company can hold, however, the true ownership of the various sister companies is often kept secret so they appear as separate parents on the applications and the laws regulating concession size can be circumvented. The following box presents the various forest harvesting licences issued by the forestry administration.

3.2 Industrial clear-cutting for pulp plantations

Indonesia's pulp and paper industry has experienced a spectacular growth over the past decade. National pulp production capacity has grown from 606,000 tonnes in 1988 to 4.9 million tonnes in 1999, i.e. an increase by 700%, while the paper industry's processing capacity rose from 1.2 million to 8.3 million tonnes annually.¹¹ As a result, the country has become the world's 9th largest pulp and 12th largest paper producer in 2001.¹²

The growth in production capacity was not matched by efforts to secure a

Forest Harvesting Licenses

There are several types of licenses that may be granted to parties to exploit forest lands. The main ones are: HPH (Hak Pengusahaan Hutan), HTI (Hutan Tanaman Industri) and IPK (Ijin Pemanfaatan Kayu).

- HPH: A license that is granted for the selective harvest of natural forests over a given period, typically 20 years and renewable for another 20 years. The license intends to maintain the forest as permanent production forest, assumes a 35 year forest recovery cycle and only allows harvesting of trees with more than 50cm DBH. HPH licenses should prevent land degradation and do not allow clear-cutting without partial replanting. A special form of logging permit is the HPHk (kecil = small), which applies to small, 100 ha concessions and can be granted by the district administrator, e.g. to village companies. The original purpose of this license was to increase local incomes and discourage illegal logging. In some areas, however, these permits have been issued in large numbers and with no planning or control, proving to be as damaging as the old-style large HPHs.

- HTI: A license to grow an industrial timber or wood plantation to supply timber or fiber, usually pulpwood. The license is valid for a period of 35 years beyond the rotation period of the main silvicultural species, renewable for another 35 years. Licensees are allowed to convert only 80 percent of the land area, 20% of natural forest have to remain as green belts and infrastructure. This limited planting requirement is not always met. Industrial forests are supposed to be established on degraded land, i.e. forests with a timber volume of less than 20 m³ per hectare as per a Ministry of Forestry Decree from 2000, but in practice they are often established after clear-cutting natural forest. The controversy about the definition of the word "degraded" between timber and conservation groups runs high. The timber industry maintains

that a forest that has few if any cash value trees left is degraded. Conservation groups maintain that a forest that has saplings and young trees with the original mature forest species composition will grow back to its original state and cannot possibly be considered degraded. Especially, if a "degraded" classification means the forest can be clear-felled and converted to monoculture tree farms. HTIs were expected by the government to supply raw materials for the pulp and paper industry, which otherwise would have been taken from natural forests. In reality, however, planting schemes have not met the minimum of 25%, which has resulted in an ongoing heavy reliance on natural forests.

- IPK: IPKs are permits to utilise the wood which is released by clear-felling forests slated for conversion to agricultural (especially oil palm) or industrial wood plantations. The costs of these permits are minimal, making mixed hardwood extraction very attractive to concessionaires that should primarily be interested in establishing plantations for other purposes. Before the recent decentralisation process, concession licenses were issued by the Ministry of Forestry in Jakarta. A decree from November 2000 permitted local governments to issue HPHk licenses. In May 2001, another decree was announced that would allow district heads to issue full-scale logging concessions. The following Megawati government, however, expressed its opposition to this decree and pledged to regain central government control over the country's forest resources. A new decree in early 2002 banned provinces and districts again from issuing licenses, but the situation remains confused because of the absence of implementing regulations for the new Forestry Law and the unwillingness at local government levels to return recently gained power back to the central government

Source: FWI/GFW, 2002 and Down to Earth, 2002.

legal and sustainable supply of raw materials, and this has proved to be devastating for the country's natural forests. Of all wood consumed by the pulp industry between 1988 and 1999, less than 8% came from plantations, most of the rest was supplied by clearing natural forest.¹³ Plantations imply investment and maintenance costs, whereas in the Indonesian policy context wood from natural forest is much cheaper, especially when it can easily be obtained illegally.

Ironically, the Indonesian government has allocated almost five times the area which would be sufficient to source the industry with plantation pulpwood, to plantation companies under the HTI program (against 1.1 million ha that would be enough if the current industry would operate sustainably). This suggests that the expansion policy was driven by a desire to make large volumes of hardwood from natural forests available to pulp producers with IPK clearance permits, regardless of whether the areas would ever be replanted.¹⁴

The growth of the pulp and paper industry has been fuelled by massive injections of capital investment of between US\$ 12 bln. and US\$ 15 bln. Foreign financial institutions made these investments with apparently little concern for the legality and sustainability of the supply of raw materials. As a result, these institutions not only took enormous financial risks, but must also accept indirect responsibility for the destruction of Indonesia's forests.¹⁵

The pulp and paper industry has been responsible for the deforestation of almost 835,000 ha of tropical rainforest in Sumatra. Almost all of this area was cleared to supply four large mills, which include the world's two biggest pulp mills, located within a distance of 100 km of each other in Riau province. In 2000, these two megamills, Riau Andalan Pulp and Paper (RAPP) and Indah Kiat Pulp and Paper (IKPP) consumed 5.7 and 8.8 million m³ of wood, respectively. Wood produced in Riau's acacia plantations is not sufficient to feed the pulp mills and covered in 2000 no more than 30% of the mills'

Some basic information on pulp and paper

The pulp & paper production chain starts with the sourcing of fiber, either by clear-cutting natural forests or from dedicated pulpwood plantations. The fiber is transported to a pulp mill, which turns the fiber into bleached hardwood kraft (BHK) pulp. In Indonesia, imported softwood pulp is often added to produce a pulp mix for higher quality paper. Pulp is traded world-wide and margins are low. Pulp mills need to be large-scale to be able to profit from the economy of scale. This means that one profitable pulp mill may require over US\$1 billion in investments.

The pulp is being sold to producers of all kinds of paper and packaging materials. Depending on the type of paper or packaging product, these facilities can be relatively small-scale.

Source : Van Gelder, 2001; Stuewe, pers.comm.

capacities.¹⁶ Most of the pulpwood therefore came from natural tropical forests such as Tesso Nilo. A study by AREAS Riau found that about 900 m³ timber a day was transported from the Tesso Nilo forest complex to the two pulp mills in early 2001. The mills' wood consumption was the equivalent of about half of all of Indonesia's legal wood supply.¹⁷ It was about double that of Riau's legal timber production from natural forests which amounted to only 6 million m³ in 1999.¹⁸ Where did the wood come from? Company profiles and a description of activities of RAPP and IKPP are presented in chapter 4.

The current overcapacity of these pulp mills is a clear example of a growth process based on 'perverse incentives' that was started under the Suharto regime.¹⁹ Once the high-capacity mills had been established, pulp and paper companies had to aim for the highest possible production level to pay off their massive debts to foreign investors. Revenues were siphoned off by puppet companies. IBRA (Indonesian

Some basic information on oil palm

To establish an oil palm plantation, a company will set up a nursery, construct roads and clear the land. All vegetation is removed. Any timber that is not considered valuable enough, e.g. where a first round of logging has taken place, will be sold to pulp mills where available, burnt, because this is the cheapest method of land clearing, or mechanically removed, where non-burning laws are enforced. In Indonesia mechanical clearing is on average 2.3 time more expensive. Often, labour is brought in from other regions. Three years after planting the palms are already productive. The costs of establishing an oil palm plantation vary between US\$ 2,500 – 3,500 per ha, most

of which the company would normally need to raise externally. When established in primary forest areas, the sale of the cleared timber might generate the funds required to establish the plantation. Oil palm fruits must be processed within 24 hours after harvesting, which requires that processing mills are close by, often inside the plantation area and the area must be made well accessible. No other plant produces a higher yield of edible oils than the oil palm: per ha yields can be 10 times higher than those of soybean. However, the yields in plantations are commonly far below optimal levels, particularly in developing countries such as Indonesia.

Bank Restructuring Agency) and international government credit agencies had to bail out these companies. The mills and their owners were thus ultimately financed by Indonesian and foreign tax payers. They became everybody's business.

3.3 Oil palm plantations

According to Oil World, the leading market research institute for the palm oil sector based in Germany, the world demand for palm oil was forecasted to increase from 22,500,000 tonnes in

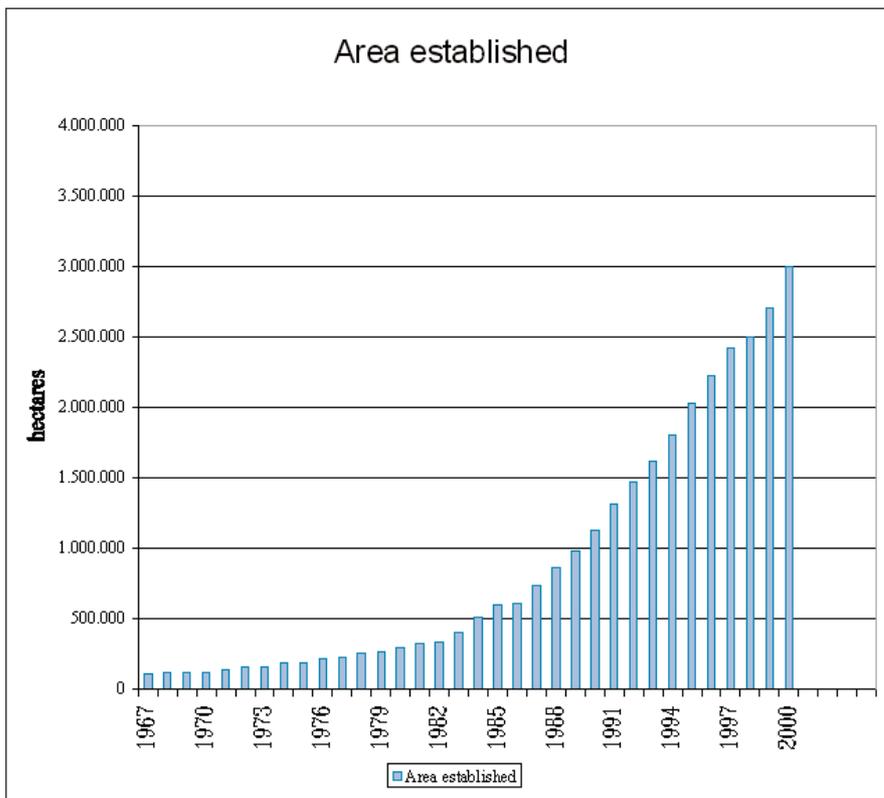


Figure 4. Expansion of the area of oil palm planted in Indonesia (1967-2000). Based on Wakker, 2000.

1999 to 40,000,000 tonnes in 2020. If this demand is to be met, producer countries will have to plant around 6 million ha of new estates until 2020.²⁰ The EU-supported Forest Fire Prevention and Control Project (FFPCP) predicts that about 50% of new plantation land will come from within Indonesia, with Sumatra absorbing most of this expansion (1.6 million ha).²¹

From the mid-1980s onward, Indonesia has already experienced a spectacular expansion of oil palm plantations. Starting from 0.6 Mha in 1985, the planted area reached about 1.0 Mha in 1990 and around 3.0 Mha in 2000 (Figure 4).

In 2001, Indonesia accounted for 32% of global production and 29% of global exports of oil palm products (crude palm oil, palm kernel oil and palm kernel meal), being the world's second producer, after Malaysia. The biggest importers of Indonesia's crude palm oil (CPO) in 2001 were India (29%), China (11%), Netherlands (8%) and Germany (5%). Germany is the Number One importer of palm kernel oil (PKO). It imports 28% of all of Indonesia's PKO exports. Indonesia supplies 85% of all German PKO imports.²²

The success of oil palm cultivation in economic terms has led to the belief that this crop would bring quick benefits for small farmers as well. In fact, all types of small-scale forest users, both (former) shifting agriculturists, transmigrants, even former hunters/gatherers regard planting oil palm seedlings as a way forward to economic prosperity. However, the Indonesian government, backed by international financial institutions and commercial conglomerates, has been pushing the large-scale industrial and not a small-scale diversified model.

Indonesia's palm oil industry is dominated by a small number of large conglomerates.²³ Some of them (notably Salim, Sinar Mas, Raja Garuda Mas and Surya Dumai) also hold major logging concessions, thus linking large scale forest clearance, wood supply and plantation establishment under one company umbrella.²⁴ Both the Raja

Garuda Mas and the Sinar Mas groups have a strong presence in the Tesso Nilo area (see section 4.2.3 for corporate diagram). Foreign investments in oil palm are considerable: in 1998 total foreign investments valued US\$3 billion.²⁵ Indonesia's state-owned forestry companies, such as Inhutani IV, are also increasingly involved in the oil palm business.

Riau is now Indonesia's leading province for the area of land under oil palms.²⁶ However, it is not yet leading in terms of production, because much of the planted area is still immature. The business is so attractive that many rubber smallholders have started to clear old rubber holdings and convert them to oil palm.²⁷

3.4 Illegal logging

Surveys by Forest Watch Indonesia, Global Forest Watch and the World Resources Institute in 2000 showed that 50-70% of Indonesia's total wood supply was obtained illegally.²⁸ Illegal logging in the country is a complex issue, which involves industries, communities, politicians, bureaucrats, military personnel and buyers.

The 2002 Annual Report of Transparency International²⁹, the world's leading NGO documenting and exposing corruption, now lists Indonesia among the eight most corrupt countries. A symptom of Indonesia's institutional and economic crisis, the rise in corruption is one of the main factors that allow illegal logging to thrive.

In general, there are two kinds of illegal logging with a large grey zone in between. The first is carried out by legitimate operators who violate the terms of their licenses. The second involves timber theft, whereby trees are felled by people who have no legal right to cut down trees whatsoever.

WWF-AREAS found both kinds of illegal logging to be common in Tesso Nilo. In December 2000, the project detected 47 illegal sawmills in and around the area. In all but one case, the owner could easily be identified. Many operators not only owned the sawmill but al-

so bought timber directly from local communities. Thirty-four separate logging groups operating in the Tesso Nilo forest at the time of the survey were identified, 28 of them were local, the others came from Jambi, Pekanbaru and North Sumatra. The groups employed 277 people. During the six-day survey period, both legal and illegal logging trucks that left the Tesso Nilo forest complex were recorded. The extracted volume was estimated at 1,670 m³ a day, 87% of which the survey team believed to be illegally harvested.³⁰

Figure 5 models a deforestation scenario for the Tesso Nilo Forest Complex assuming illegal logging continues at the 2000 rates.

In the WWF-AREAS survey, about 63% of the total wood taken from the Tesso Nilo area was most likely destined for pulp mills. Investigations revealed that one of the mega pulp mills, Indah Kiat, was actually buying illegally obtained wood from former fishermen that had been forced to give up fishing due to pollution created by the same mill. As one fisherman stated, *"now there are no fish left. They have all been poisoned by the factory, so chopping down the forest is the only way we can make money."*³¹

Factors that facilitate illegal logging in the Tesso Nilo area are³²:

- the resource -round logs, plywood timber, pulp timber- is readily available.
- the infrastructure necessary to illegally harvest timber even without heavy equipment was created by the legal logging operations and has been ingeniously modified by the local gangs.
- a market that buys the contraband and encourages its harvest exists.
- laws regulating timber harvest are not enforced.

There are five main players in the illegal logging game³³:

- *villages* provide labor and organize small harvesting operations; this includes traditional, transmigration and refugee villages. Villagers participate because of the economic crisis which

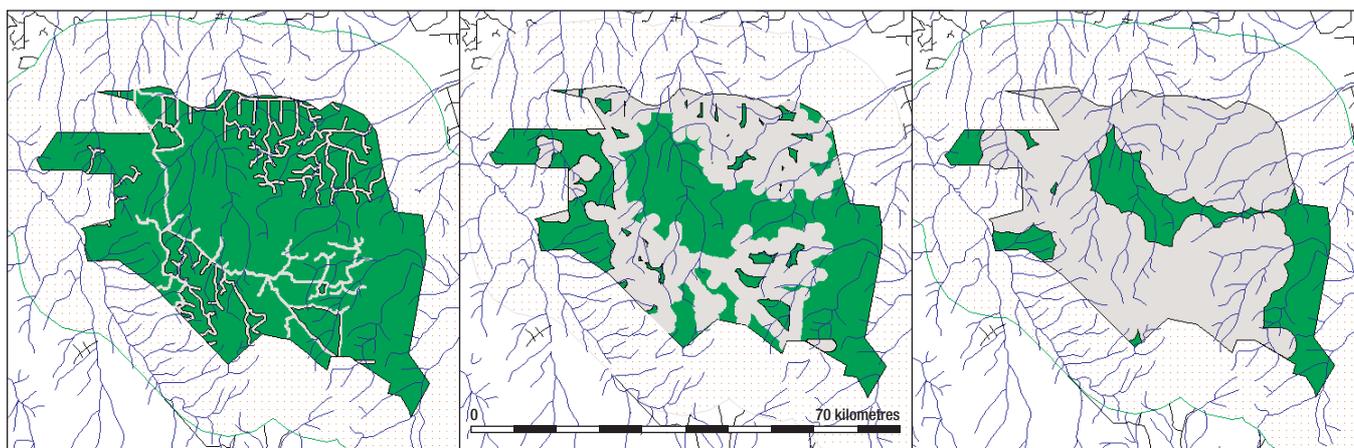


Figure 5. Projection of the potential impact of illegal logging on the Tesso Nilo Forest Complex should logging continue at 2000 rates (for year 2001, 2004 and 2006). The model assumes illegal logging to advance at increasing distances from existing logging roads; dark grey = forest, light grey = severely degraded due to advance of illegal logging (Martin Hardiono, WWF-AREAS, December 2001).

led to increasing poverty, because they see an overall breakdown of the rule of law and do not want outsiders to profit from ‘their’ resources, and because of land right and resource access conflicts they fear they will lose anyway.

- “mobsters” organise gangs at the province level which provide funds and hire labour either from villages or from a refugee community.
- *military, police, and other enforcement personnel* provide protection, transport and sometimes funding to run operations.
- *government officials* provide illegal or “grey” permits to conduct some of the operations.
- *companies* “encourage” illegal operations to be able to buy feed stock for their pulp and plywood factories.

Illegal logging operations use so-called “brokers” as intermediaries between processing mills and loggers. They are assumed to be employees of local or provincial authorities or just people from the villages. The logging gangs are mostly made up of around five loggers, sometimes migrants from northern Sumatra that live in illegal camps in the forests, easy to be seen by legal companies and forest police but working undisturbed. Each team member earns around 28.000 Rupiah per day after paying the broker’s fee and for the transport. That is slightly more than the average employee of RAPP earns.³⁴

4. Main players behind the threats

4.1 Indonesian Government Agencies

The decentralisation context

In May 1998, the autocratic Suharto Regime was replaced by a new government. The regime change seriously affected the political structures in the country. The role of various levels of government in the Tesso Nilo area changed dramatically as the new government began a decentralisation process. This process towards regional autonomy rapidly and often chaotically shifted power from the centre to the provinces and districts. That affected many functions of government, including land use planning, and forest policy and management. The changes present both opportunities and risks for forest conservation.³⁵

Democratisation and decentralisation allowed previously marginalized players such as environmental NGO's, rural communities, local authorities, religious leaders and academics to have a voice in the formulation of natural resource policies. Decision-making was handed down to district authorities who may be more aware of the local social context and may be more ready to listen to local communities whose livelihood interests are directly at stake.

District heads were given the right to hand out small logging concessions (HPHk). In some areas they have done so in large numbers without any land use policy in place. Many were eager for license fees in the absence of reliable income sources to cover their budgets. Others simply felt their time had come to benefit from the exploitation of forest resources. In many cases, the result was accelerated forest degradation and deforestation. A new decree by the Ministry of Forestry in October 2000 tried to stop this practice but was ignored in many areas.

In May 2001, a decree was announced that would have allowed district heads to issue full-scale logging concessions and would have handed them considerable power to manage protected forest areas. The incoming Megawati government, however, expressed its opposition to this decree and

pledged to regain central government control over the country's forest resources. A new decree in early 2002 banned provinces and districts again from issuing licenses. This re-centralisation of power was complicated by the fact that provincial and district officials had already tasted the power and profits that come with local control over forest and other natural resources and consequently were not ready to give away that recently gained power. Such power conflicts and confusion over who has the authority created a "get-what-you-want-before-it-is-too-late" atmosphere, resulting in accelerating forest loss.

Disputes also arose over the degree to which local land use plans could be overruled by central government planning and about which level of government has the authority to change the status of forest lands, e.g. from protection to production forest where timber may be harvested selectively from natural forest stands, or from production to conversion forest where natural forest may be cleared and converted to industrial wood or estate crop plantations. Many provincial land use plans tended to increase the amount of forest classified as conversion forest at the expense of production forest in comparison with plans and maps prepared by the Ministry at the national level. The provinces claim that their plans reflect the situation on the ground more accurately, but they make it easier to have logged-over forest cleared for oil palm and pulpwood plantations.³⁶

Also in the case of Riau, there has been some arm wrestling between the central and provincial governments as to which of the land use plans prepared at either level was valid. The Ministry of Forestry claims that Riau has more production forest than the provincial land use plan indicates. In 2000, almost 1.6 million ha of production forest had been rezoned as conversion forest in Riau (18% of the province's mainland area); 1.1 million ha were being processed but large areas were disallowed because many claims were found to overlap, a symptom for the high demand for forest conversion in this province.³⁷

On the other hand, provincial planning authorities have also been in favour of placing more forest land under protection, especially the peat forests near the coast that prove to be very vulnerable to protracted burning after clearing.

The agencies involved

The main government institution determining the fate of Tesso Nilo is the Ministry of Forestry (MoF), which has the right to declare Tesso Nilo a protected area, but which also issues logging and conversion permits. Chapter 2 has presented the latest developments as to the designation of forest lands in and around Tesso Nilo.

Within the Ministry, three directorate generals (DG) are most involved:

- "Forest Protection and Nature Conservation", which would formally manage the Tesso Nilo protected area, once it receives legal protected status; this DG has applied for such a declaration.

- "Forest Planning", which evaluates the application; this bureau appears to be in favour of declaring the Tesso Nilo forest a protected area.

- "Production Forests", which is in charge of the Tesso Nilo forests. A change in land use status would mean that "their" area would have to be handed over to "Forest Protection and Nature Conservation". The DG of Production Forests has not yet made up its mind, but appears to be conservative.

KSDA-Riau³⁸ is MoF's executing agency in the province. Daily management of the protected area would be delegated to this agency, unless it is ranked as a national park which is managed by central agencies. KSDA duties include curbing illegal activities, unless there is an agreement for joint management by several parties. However, the poorly staffed and funded KSDA has not been very successful in effectively protecting other protected areas in Riau against encroachment, illegal logging and monitoring overlapping concessions. Some of its main and most controversial duties at the moment appear to be to provide help to farmers and plantations that are being raided by elephants and to maintain a population of captured crop-raiders.

The Riau Forest Service is a provincial government agency that manages and controls all non-protected forests and has shown similar weaknesses as the KSDA. It is in charge of controlling illegal logging outside of protected areas but appears to have little control over it. The Riau Planning Board facilitates the creation of land use plans, and in 2002 floated a highly controversial new plan to replace the old 25-year plan.

The Riau Governor's office is trying to boost revenue and to provide employment opportunities in the province and is therefore interested in re-designating more and more areas for commercial use. Still, it has endorsed the protection of Tesso Nilo.

District governments and parliaments have expressed their support to a Tesso Nilo Protected Area in general terms, but they are also constantly being lobbied by businesses and communities to open more forest for logging or conversion.

4.2 Indonesian companies

Indonesian exports in general

Indonesian government statistics for 2001 show the top ten export destinations for non-oil & gas products. The USA was the number one destination, taking a 17% share of total export value. The next were five Asian countries, which together imported 37% of the total export value. They were followed by three EU countries: the Netherlands, the UK and Germany, ranking 7, 8 and 9, respectively. Together, the three EU countries accounted for almost 10% of Indonesia's export value from the non-oil sectors.³⁹

Riau is said to be one of the richest provinces in Indonesia, economically. This is largely due to vast crude oil and gas production along Riau's coast line. The oil is produced by Caltex, a Chevron and Texaco collaboration, and value is added by the state owned refinery Pertamina. Profit sharing in the oil revenues has always been a contentious issue between the central and provincial government, most profits went into cen-

tral government's coffers. After a lot of "independence" talk in the province, in January 2002, the governor of Riau with the blessing of the central government signed a first "new" deal that will give the province a 50% share in the profits of one of the oil fields that had been up for re-negotiation.⁴⁰

Riau also occupies a front position regarding its provincial share of non-oil-and-gas national exports. Riau ranks third among 27 Indonesian provinces, accounting for 12.5% of the country's non-oil-and-gas export value. In volume, Riau even has a number one position, with 94 million tonnes of non-oil-and-gas exports⁴¹, that is 45% of Indonesia's total export volume. Second and third placed South and East Kalimantan together account for another 31% of the national export volume.⁴² Most of Riau's non-oil-and-gas is from industries that depend on the conversion of its forests.

4.2.1 Pulp & Paper companies

Mega-mills

Two integrated pulp and paper mill complexes are located in Riau less than 100 km distance from each another and from the Tesso Nilo forest:

1. *IKPP/AA* (Indah Kiat Pulp and Paper owns the pulp and paper mill, Arara Abadi owns the pulp-wood concessions), and
2. *RAPP/RAK* (Riau Andalan Pulp and Paper owns the pulp mill and pulp-wood concessions, Riau Andalan Kertas owns the associated paper mill).

Together, these two operations account for ca. 60% of Indonesia's total pulp production⁴³ and rank among the largest stand-alone pulp production facilities in the world.⁴⁴ These two companies are, without doubt, the most significant players from the private sector that determine the fate of the Tesso Nilo landscape and other high conservation value forests in Riau. The two mills are related to all other pulpwood concession owners in the Tesso Nilo area, either through joint venture partnerships or through third party delivery con-

tracts. Most of these relationships are kept secret because of competition between the two mills but also because of laws governing the size of land any given corporate entity and its clan of companies can hold.

Riau's industries consumed 16 million m³ of wood in 1999.⁴⁵ Of that, the Indah Kiat and RAPP mills accounted for roughly two-thirds, ca. 11 million m³. That alone is almost double the 6 million m³ of natural wood that could legally be harvested in Riau that year: 1.5 million from HPH timber concessions and 4.3 million through forest conversion permits.⁴⁶ These figures clearly show the absolutely dramatic effect these two mills have on Riau's natural forests and how much their simple existence appears to have been encouraging illegal logging and forest conversion.

Both mills, especially RAPP's, now cover part of their fiber needs from acacia plantations bordering the Tesso Nilo forest. But both still rely mainly on natural wood from forest conversion in their own concessions and in those of third parties and joint venture partners. Some of those clear-fell inside Tesso Nilo and inside the Tesso Nilo landscape, sometimes without proper permits. Based on data provided by the two companies, Barr (2002) calculated that both will eventually be able to satisfy up to 50% of their mills' capacities with plantation wood generated from their own concessions (see graphs in figures 6 and 7). The remaining 50% will initially be covered by mixed tropical hardwood (MTH) and later by plantation acacia from third party or joint venture (JV) sources. Yield projections by the companies for their own pulpwood plantations have proven to be over-optimistic time and again. Still the discussion about percentages of mill capacity covered by plantation wood or by MTH misses one critical point: analysis of historical sequences of satellite images clearly show that most plantations operated by the mills today were tropical forest yesterday.

The mills' pulpwood needs present an enormous pressure on Riau's few remaining natural forests and are consid-

ered by some to be a major drive for illegal logging operations: a CIFOR study estimates that Indonesian pulp producers may have obtained as much as 40% of the wood they consumed between 1994 and 1999 from illegal sources.⁴⁷ Indah Kiat and RAPP claim that their mills will be exclusively supplied by plantation wood by 2009 and 2007, respectively (Fig. 6 and Fig. 7). To reach those targets, the companies plan to convert 200.000 to 240.000 ha of natural forest, each mainly in peat swamps, the only forest type remaining in sufficiently large blocks. However, conversion rights to these lands have not yet been fully secured. In the meantime, RAPP and Indah Kiat run several operational and financial risks in pursuing their 'sustainability' targets⁴⁸:

- 1) Continued heavy reliance on the conversion of natural forest further away, at increased costs, until expansion into peat swamps is secured.
- 2) Technical challenges and ecological risks associated with plantation development in peatlands.
- 3) Social conflicts, because those lands are claimed by local people, and the uncertainties surrounding regional autonomy.
- 4) Financial constraints for new investments because of the companies' heavy debt loads.
- 5) Extremely optimistic projections of planting rates and production volumes on their plantations.

Public interest in the destructive impacts of the Indonesian pulp and paper industry as a result of NGO campaigns in consumer countries has not gone unnoticed by the conglomerates. It is felt as a threat to the ability to market their products in some countries. As a result, companies such as APP and APRIL have designed marketing strategies to obscure their identity as the original manufacturer of the paper. As part of its promotion strategy, APRIL falsely claims that it clears degraded forest and that its forestry operations help preserve biodiversity⁴⁹, whereas there is ample evidence that many of the forest areas being cleared, such as Tesso Nilo, are in fact High Conservation Value Forests.

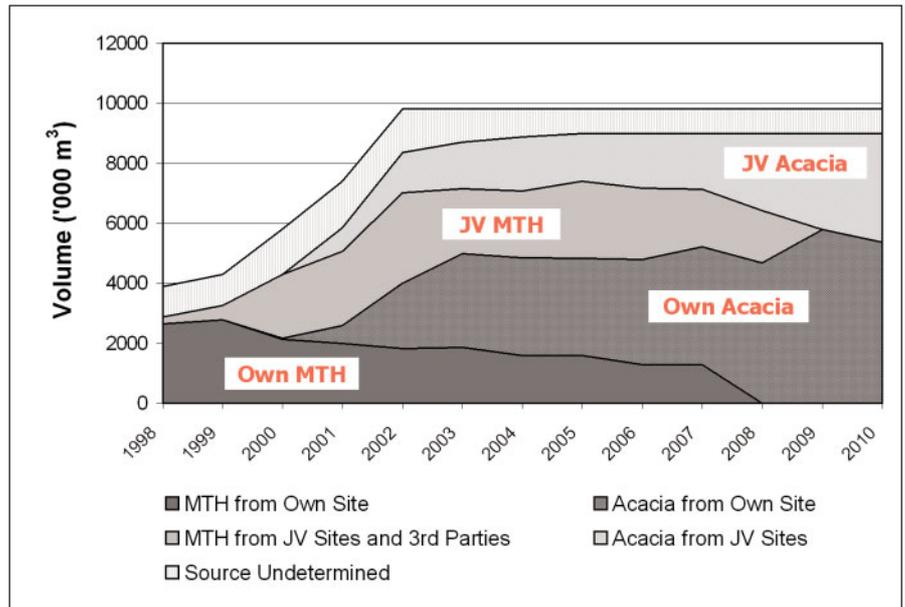


Figure 6. RAPP Wood Supply Plan from All Sources (Barr, 2002).

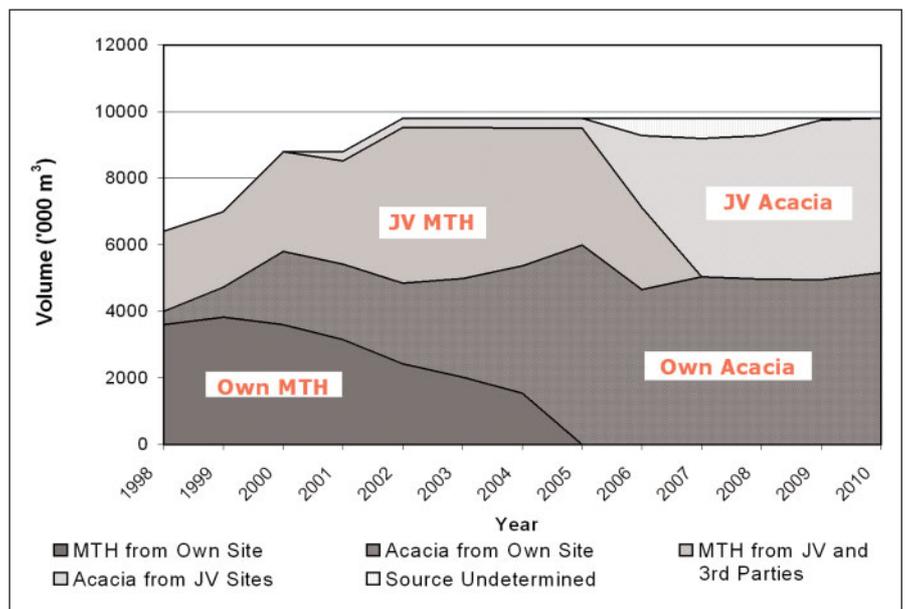


Figure 7. Indah Kiat Wood Supply Plan from All Sources (Barr, 2002).

In addition to the pulp wood concessions directly owned by RAPP and Arara Abadi, three other companies own timber concessions along the border of the proposed TNPA:

- PT Rimba Lazuardi
- PT Rimba Peranap Indah
- PT Nusa Warna Raya.

Some of them have or are negotiating contracts as third party suppliers, joint venture partners, or are take-over

targets. Figure 3 shows the pulpwood concessions (HTI) around the Tesso Nilo forest.

Company profile: Riau Andalan Pulp & Paper (RAPP), Riau Andalan Kertas (RAK)

Parent group: Raja Garuda Mas

PT Riau Andalan Pulp & Paper is 98.5% owned by Asia Pacific Resources International Holdings Ltd. (APRIL) in Singapore. PT Riau Andalan Kertas is 99.8% owned by APRIL.

APRIL is part of the Indonesian Raja Garuda Mas Group (RGM), which is ultimately owned by Sukanto Tanoto and his family. RGM is active in agribusiness, forestry, pulp & paper, steel, chemicals, finance, trading, mining, property and services.⁵⁰

Key data

• Production capacities

The pulp mill of PT Riau Andalan Pulp & Paper (RAPP) in Kerinci (Riau) has an annual production capacity of 2,000,000 tonnes of bleached hardwood kraft pulp, making it one of the largest pulp mills in the world.

The associated paper mill of PT Riau Andalan Kertas (RAK) has an annual production capacity of 350,000 tonnes.⁵¹

• Consumer products

Printing and writing paper (63%), boards and coated paper (24%), tissue (8%), and other paper (5%).⁵²

• Brand Names

PaperOne, Copy & Laser, Crystal Copy, Perfect Copy, Dunia Mas.

• Financial figures

In 2000, APRIL realised a turnover of US\$ 652.3 million. Of this turnover, 59.6% was attributable to pulp and 40.4% to paper. Exports accounted for 85.1% of the turnover. The main export markets are Asia, the Middle East, and Europe.⁵³

Foreign financial involvement

Foreign financial institutions have helped finance the strong expansion of Riau Andalan Pulp & Paper, Riau Andalan Kertas and their parent company APRIL by issuing shares and bonds, buying their shares and bonds, providing loans, and extending credit guarantees. German financial institutions did not play a significant role in this respect.⁵⁴

Because of the Asian financial crisis APRIL ran into financial trouble at the end of the 1990s. The company and its subsidiaries had to restructure most of their US\$ 1.3 billion debt. Still they were looking for capital to expand annual pulp production from 850,000 to 2 million tonnes and to double paper production from 350,000 to 700,000 tonnes per year.

• In September 1997, PT Riau Andalan Kertas secured a total loan package of US\$ 436 million from an international banking consortium, advised by Barclays Bank (United

Kingdom) and Macquarie Bank (Australia). The loan package was meant to finance a second paper line, which would double annual capacity to 350,000 tonnes. The loan package was partially guaranteed by the export credit agencies of Sweden, Finland and Germany (Hermes Kreditversicherung), as companies from these countries would supply machinery for the second paper line. But when the Asian financial crisis broke out at the end of 1997, the loan package was put on hold by the banks and/or the export credit agencies. Early 1998 the loan package was cancelled entirely. Lacking sufficient funds, Riau Andalan Kertas today still has not established a second paper line.⁵⁵

• The Finnish company UPM-Kymmene in September 1999 terminated its strategic alliance with APRIL, when it became clear that APRIL would not succeed in bringing its second paper machine in Riau on-line before the end of 1999. The strategic alliance of January 1998 had meant to bring the entire paper production of the two companies under joint control as APRIL expanded its paper production in Riau and Changshu (China).⁵⁶

As part of the alliance UPM-Kymmene had taken a 49% share in APRIL's fine paper and stationery companies in Changshu and Suzhou (China) in March 1998, and had advanced a US\$ 121 million loan to APRIL in December 1998. These two commercial ties between the two companies continued to exist after September 1999.⁵⁷

• In June 2000, APRIL signed a debt restructuring agreement with its Indonesian creditors headed by the Indonesian Bank Restructuring Agency (IBRA), which had taken over the bad loans of some commercial banks. Around US\$ 800 million of RAPP and RAK debt was restructured. The agreement extended these loans to the end of 2005. It allowed APRIL to defer interest payments for a maximum of US\$ 160 million until March 2001, to assist in financing the completion of the first phase of the second pulp line at RAK. Such an arrangement is unusual and therefore the IBRA first objected to the deal which had already been signed by the Indonesian banks in September 1999. Only when IBRA-chief Glenn Yusuf was replaced by Cacuk Sudarijanto the government agency changed its position and also signed the agreement.

Several members of the Indonesian parliament, as well as foreign creditors of APRIL, criticised the fact that IBRA signed this debt restructuring agreement. The foreign creditors, headed by ING Barings (United Kingdom), a subsidiary of ING Bank (The Netherlands), refused to sign. The foreign creditors have total loans of US\$ 117.8 million outstanding to APRIL.⁵⁸

• In August 2000, APRIL agreed to sell its 51% interest in the Changshu paper mill to UPM-Kymmene for US\$ 150 million, to raise money for the expansion of its Riau pulp mill. That gave UPM-Kymmene full ownership. The converting plant in Suzhou was transferred to APRIL. APRIL will al-

so continue to hold the US\$ 121 million loan from UPM-Kymmene and the loan's new collateral now is formed by approximately 12 percent of PT Riau Andalan Pulp & Paper's shares.⁵⁹

- In October 2000 United City Bank (Unibank) was put under the control of the Indonesian Bank Restructuring Agency (IBRA). Unibank was the banking subsidiary of the Raja Garuda Mas Group and had lent hundreds of millions of dollars to companies within the Raja Garuda Mas Group, such as APRIL. Many of these loans were not repaid, bringing Unibank into trouble. Despite efforts by IBRA to revive the bank, it was closed down at the end of October 2001 by Bank of Indonesia, the Indonesian central bank. Unibank's closure left the IBRA with the obligation to pay back around US\$ 230 million to the customers of the bank. The IBRA tried to hold Sukanto Tanoto responsible for the repayment, but Mr. Tanoto had sold its shareholdings in the bank to a number of new owners as early as 1999. The share-owners, which are unknown to the Bank of Indonesia, are believed to be fronts for Mr. Tanoto.⁶⁰

- Despite the favourable terms of its June 2000 debt restructuring, APRIL soon ran into trouble again when world pulp prices collapsed. In February 2001, APRIL asked its creditors to revise the debt restructuring agreement. APRIL asked lenders to grant a three-year grace period for the repayment of principal and to extend repayment until 2012. It also wanted lower interest charged on the loans. Creditors were balking, as APRIL at the same time invested large sums into an expansion of its pulp production in RAPP.⁶¹ This was made possible in part because of UPM-Kymmene had bought APRIL's share in their joint Chinese mill.

- In March 2001, APRIL's subsidiaries defaulted on the first scheduled principal repayment for the month of March 2001. Interest was again being paid.⁶²

- In June 2001, APRIL announced that it could not meet interest payments on its debts because of a steep decline in pulp prices. Again, the company began discussing a debt restructuring with its creditors.⁶³

- In September 2001, the New York Stock Exchange suspended trading in shares of Asia Pacific Resources International Holdings Ltd., because the price of APRIL's shares had traded below US\$ 1 over a 30-day period. The company had been listed on the NYSE since April 1995. Instead, APRIL started trading its shares on the American over-the-counter Bulletin Board at the end of September 2001.⁶⁴

- In April 2002 APRIL reported that discussions with its creditors on the restructuring of its US\$ 1.2 billion debt were still going on. Some lenders had not signed and were asking for better terms.⁶⁵

- In April 2002, UPM-Kymmene and APRIL agreed upon a restructuring of UPM's US\$ 121 million loan to APRIL. The loan will now be repaid through regular instalments, first of which was paid in April 2002. The final maturity of the loan was extended until December 31, 2006. Shares in PT Riau Andalan Pulp & Paper would continue as collateral for the loan.⁶⁶

Fibre supply

From 1995, the start of pulp production, to 2000, RAPP's pulp production relied fully on the clearance of natural forests for its fibre supply. It is estimated that by the end of 2001 Riau Andalan Pulp & Paper had cleared 220,000 hectares of rainforest. By the company's own estimates, it will be clearing an additional 147,000 hectares of rainforest until 2008, but this probably is strongly under-estimated.⁶⁷

The Raja Garuda Mas Group holds a plantation concession with a gross area of 280,500 hectares in Riau, which will be used to supply Riau Andalan Pulp & Paper's mill. Excluding areas reserved for infrastructure and natural forest, the net plantable area is 192,000 hectares. Furthermore, the company has access to a net plantable area of 138,000 hectares held by associated and joint-venture companies and a net plantable area of 20,000 hectares managed by nearby communities as part of an out-grower scheme. The total planned plantation area therefore is 350,000 hectares. The company claims that in mid-2002 an area of 171,000 hectares had been planted on all these sites.⁶⁸

Harvesting of the company's plantations started in 2001 and supplied 20% of fibre needs in that year. According to the company this percentage should increase to 100% in 2008.⁶⁹

The company claims that an annual output of 2 million tonnes of pulp would require 9 million tonnes of acacia. It expects annual yields of 126-315 m³/hectare in a seven year rotation period. When the company succeeds in actually planting 350,000 hectares (50,000 hectares per year), this would yield an annual production of somewhere between 6.3 and 15.8 million tonnes of acacia. That is: between 70 and 175% of its total fibre need. So even the company's own figures indicate that the plantation yield could be far (30%) below its actual fibre needs.⁷⁰

Independent analysts are less optimistic, arguing that Riau Andalan Pulp & Paper will probably need 10 million m³ of acacia to produce 2 million tonnes of pulp annually. According to studies by forestry analysts like Jaakko Poyry, an eight year rotation period and an estimated yield of 150-190 m³/hectare are more realistic parameters. Using these parameters and assuming that the total area of 350,000 hectares is planted, APRIL's plantations would have a maximum annual yield of somewhere between 6.6 and 8.3 million m³. That is: between 66 and 83% of its total fibre need.⁷¹

It therefore seems probable that Riau Andalan Pulp & Paper will be needing additional supplies to complement its insufficient yields of plantation wood, even when its plantations

are fully operational. And it must be emphasized that its plantations are far from fully operational yet. Independent analysts doubt that the company will succeed in (re)planting 50,000 hectares each year in the near future. In recent years planting rates stayed far from this goal, which means that the actual yield of APRIL's plantations will be considerably lower than projected at least until 2007. It is expected that by 2007 the plantations will supply no more than 32% of Riau Andalan Pulp & Paper's fibre need.⁷²

APRIL's supply shortfall has to be met by other supplies, quite probably by logging natural forests elsewhere. APRIL does not have many natural forest concessions outside of Tesso Nilo, it appears obvious that APRIL focused on the Tesso Nilo forest as the largest remaining patch of unconverted lowland forest in Sumatra when the company designed the plans for the pulp mill. The pulp mill is located at the Kampar river, a large navigable river that allows supplies and products to be brought in and out by ship. The river and the mill border Tesso Nilo, thus allowing for short trucking distances between the logging sites and the mill. Logging companies apparently associated with RGM began cutting the forest long before the APRIL pulp mill was built and delivered the round logs to RGM-owned sawmills. As logging operations were coming to an end, APRIL apparently applied for changes of forest status from "limited production" to "production". As they received some of the permits they had applied for, they immediately began clear-felling these forests, shipped the timber to the RAPP pulp mill and began to grow acacia on the converted land.

In 2000, RAPP began a new phase of trying to convert the core of Tesso Nilo. Maps at the Riau Forest Service show RAPP conversion permit applications right inside the natural forest, often on land for which the logging company Hutani Sola Lestari held concession rights. In July 2001, RAPP began clear-felling through the middle of the forest along the main logging road, converting natural forest to acacia plantations. Apparently anticipating, that this clearing activity would create controversy, it was backed up by huge military and police support. Ironically, these operations began after the Ministry of Forestry's KSDA office had applied to set this forest aside as a national park. Operations went on as WWF was conducting biodiversity surveys in the same area to provide baseline data for the proposed protected area. While the biologists were sampling the plot, RAPP loggers were waiting with their chain saws running. Within hours, the plot became a truly "historical data set", a case study on the history of Indonesia's forests. The results of the biodiversity surveys showed that these forests had one of the highest vascular plant diversities ever recorded in the world. RAPP would later claim that they were only converting "degraded" forest. The company argued that it had permits for these operations but until today has refused to show them.

RAPP today claims that it planted acacia along the logging corridor to prevent encroachment of the surrounding natural forest by villagers. However, RAPP had no official legal interest in that forest. And the company's maps seem to show a

different story. One kilometer wide strip acacia strips link existing RAPP acacia plantations and divide the remaining Tesso Nilo forest into three distinct sections, each bordering an existing major RAPP acacia plantation (see figure 3). The remaining forest appears to be readily parcelled to convert one at a time in a next round of applications for change of status due to "degradation".

Another point of frequent criticism concerns the way in which Riau Andalan Pulp & Paper treats the land rights of the indigenous communities in its concession area. A study by the independent auditors Société Générale de Surveillance (SGS), commissioned by APRIL in 1998, found that over 40,000 hectares of APRIL's concession area has been claimed by local communities. The area where the Riau Andalan Pulp & Paper factory has been built is land claimed by the indigenous people of the Delik, Sering and Kerinci villages. As a result of this dispute the legal representative of these villages was imprisoned for three years. In another land dispute case within APRIL's concession area, a member of the community of Lubuk Jambi village is reported to have been stabbed to death during a protest in 1998.⁷³ Until today, RAPP is still unable to plant acacia on some lands to which they hold concession rights because of territorial disputes.

NGO campaigns

Because of its unsustainable fibre supply, land right conflicts with local communities and disregard for the biodiversity and conservation values of the Tesso Nilo forest, APRIL has been heavily criticised by Indonesian and international NGOs. In 2001, local NGOs, WWF and Friends of the Earth asked APRIL to stop the clearing of Tesso Nilo and other forests around its concession lands.⁷⁴

The NGOs were not alone in calling on APRIL to conduct business in a more environmentally friendly way. UPM-Kymmene, one of APRIL's investors and important pulp customers, had been negotiating with APRIL on a modification of their existing loan repayment and pulp supply agreement for UPM-Kymmene's paper plant in Changshu (China). In April 2002, APRIL announced a number of environmental improvements that had been demanded by UPM-Kymmene, which had been lobbied by WWF-Finland and Friends of the Earth-Finland for many years regarding its Sumatran investments.

- RAPP announced it would conduct a third party audit by an independent auditor, concerning allegations on receiving illegally harvested wood. The audit was completed late 2002 and RAPP has promised to take corrective actions.

- RAPP also has certified six of its forest concession areas according to the ISO 14001 Environmental Management System. The company announced it would continue the process to certify the rest of the concession areas and the mills.

- In March 2002, APRIL announced a temporary moratorium on logging in the Tesso Nilo forest, while they are engaged in discussions with relevant stakeholders to find mutu-

ally acceptable solutions to preserve the biodiversity in the area.⁷⁵ From September 2002 on, APRIL also agreed not to source from outside suppliers any wood originating from Tesso Nilo.

- From September 2002 on, APRIL agreed to no longer transport trucks carrying timber without license on their company ferry.

Company profile: Indah Kiat Pulp & Paper

Parent group: Sinar Mas

PT Indah Kiat Pulp & Paper Tbk. is 58% owned by the Singaporean company Asia Pulp & Paper Company Ltd. (APP). APP is the holding company for the pulp and paper interests of the Sinar Mas Group, one of Indonesia's largest business groups. The group is mainly active in pulp & paper, palm oil, food, property development, hotels, telecommunications and finance. It is founded by the Chinese immigrant Oei Ek Tjiong, who later changed its name into Eka Tjipta Widjaja. The Widjaja family is still controlling the Sinar Mas Group.⁷⁶

The financial crisis of 1997/98 left the Sinar Mas Group relatively untouched. The group "now towers over all surviving conglomerates in Indonesia", concluded Asiamoney in July 1999. During the 1990s APP had built up an aggregate pulp production capacity of 2.3 million tonnes, located in Indonesia. Its paper and packaging production capacity in Indonesia, China and India totalled 5.7 million tonnes. In 1999, APP was the largest Asian paper producer outside Japan, and ranked 10th among the world's paper and packaging companies.⁷⁷

APP's tremendous expansion was financed mainly by foreign money. Weak due diligence procedures and unrealistic growth estimates had lured virtually all globally active financial institutions to inflate APP with a massive US\$ 13.4 billion of debt, making it the largest corporate debtor in Asia.⁷⁸

Key data

• Production capacities

PT Indah Kiat Pulp & Paper Tbk. is one of the largest producers of bleached hardwood kraft (BHK) pulp in Asia (excluding Japan), operating four BHK pulp mills in Perawang (Riau) with a combined annual production capacity of approximately 1,781,000 tonnes. The adjacent paper mill has a production capacity of 654,000 tonnes. In West-Java Indah Kiat owns a paper mill with an annual production capacity of 90,000 tonnes and a packaging board mill with an annual production capacity of 980,000 tonnes. The West-Java mills are supplied with pulp from the Riau mill.⁷⁹

• Consumer products

Coated and uncoated printing and writing papers, containerboard and boxboard.⁸⁰

• Brand Names

Sinar Spectra, Signature Bond, Golden Plus and others.

• Financial figures

Annual sales of Indah Kiat in 2001 amounted to US\$ 1,100.2 million, resulting in a net loss of US\$ 182.4 million.⁸¹

Foreign financial involvement

Foreign financial institutions have financed to a large extent the strong expansion of Indah Kiat and its parent company APP, by helping them to issue shares and bonds, by buying their shares and bonds, by providing loans, and by extending credit guarantees. German financial institutions played a significant role in all these fields:⁸²

• Buying shares of Indah Kiat

APP owns ca. 58% of PT Indah Kiat Pulp & Paper shares. The rest are owned by institutional and private investors, inside and outside Indonesia. Since APP's debt crisis broke out two years ago, many of them have dumped their shares. The following German financial institutions bought Indah Kiat shares at the end of the 1990s, thus supplying the company with part of the equity it needed for its vigorous expansion:

- Commerz International Capital Management, a subsidiary of Commerzbank
- Montgomery Asset Management (United States), a subsidiary of Commerzbank
- Union Investment
- Universal Investment
- WestLB Asset Management, a subsidiary of Westdeutsche Landesbank

• Issuing bonds for Indah Kiat

The following German banks helped Indah Kiat to issue bonds on the international capital market in the 1990s:

- Bank Austria (Austria), which now is a subsidiary of HypoVereinsbank
- Norddeutsche Landesbank

• Providing loans to Indah Kiat

The following German banks participated in bank syndicates providing loans or export credits to Indah Kiat in the 1990s :

- Bank Austria (Austria), which is now part of HypoVereinsbank
- Bankers Trust (United States), which is now part of Deutsche Bank
- Berliner Handels und Frankfurter Bank, which is now part of ING Bank (The Netherlands)
- Commerzbank
- Deutsche Bank
- Dresdner Bank
- IKB Deutsche Industriebank
- Landesbank Schleswig-Holstein
- Norddeutsche Landesbank

• Providing export credit guarantees

The German export credit agency Hermes Kreditversicherung has issued various export credit guarantees in the 1990s for loans to finance German machinery supplies to Indah Kiat.

• **Buying shares of APP**

The dominant shareholder of APP is the Widjaja family, which owns around 67% of the APP shares. The rest of its shares is owned by institutional and private investors, inside and outside Indonesia. Many of them have dumped their shares. The following German financial institutions bought APP shares at the end of the 1990s:

- Deutsche Asset Management, which is part of Deutsche Bank
- **Deutsche Postbank**
- DWS Investment, which is part of Deutsche Bank
- Zürich Scudder Investments (United States), which is part of Deutsche Bank

• **Issuing bonds for APP and its subsidiaries**

The following German banks helped APP and its subsidiaries (others than Indah Kiat) to issue bonds on the international capital market in the 1990s:

- Deutsche Morgan Grenfell (United Kingdom), which is part of Deutsche Bank
- Dresdner Bank

• **Providing loans to APP and its subsidiaries**

The following German banks participated in bank syndicates providing loans or export credits to APP and its subsidiaries (others than Indah Kiat) in the 1990s:

- Baden-Württembergischen Bank, which is part of **Landesbank Baden-Württemberg**
- Bankers Trust (United States), which is now part of **Deutsche Bank**
- **Bayerische Landesbank**
- Bayerische Vereinsbank, which is now part of **HypoVereinsbank**
- **Berliner Handels und Frankfurter Bank**, which is now part of ING Bank (The Netherlands)
- **Commerzbank**
- **Deutsche Bank**
- Dresdner Kleinwort Benson (United Kingdom), which is part of **Dresdner Bank**
- **HypoVereinsbank**
- **IKB Deutsche Industriebank**
- **Norddeutsche Landesbank**

The German banks and financial institutions were asked to comment on their involvement. Their responses are given in Annex 2.

• **Debt restructuring APP**

When global pulp prices collapsed and the growth of the Chinese paper market slowed down in 2000, APP defaulted on its debt repayments. In March 2001, APP appointed Crédit Suisse First Boston (Switzerland) to co-ordinate the restructuring of its debt. A week later, APP announced that the company and all its subsidiaries would immediately halt payment of interest and principal on all debts.⁸³

These events started complicated debt restructuring negotiations between APP and its creditors, which are still not fi-

nalised today, two years later. Some of the highlights in this process include:

- Trading of APP-shares was suspended by the New York Stock Exchange in April 2001, and APP was delisted in September 2001.⁸⁴

- In April 2001, the creditors of APP organised themselves into several committees, which would represent the different creditor groups in the debt restructuring discussions with the company. Separate committees were formed for the Chinese state banks, the commercial banks, the export credit agencies, the bondholders and the trading company creditors. Together, these committees elected an umbrella steering committee. Among its thirty members are **Deutsche Bank** and **HypoVereinsbank**.⁸⁵ **Hermes Kreditversicherung** plays a leading role.

- In May 2001, the international accounting firm KPMG was appointed as the financial advisor to the creditor committees.⁸⁶

- All APP assets in Indonesia, including Indah Kiat and Arara Abadi, were put under control of the Indonesian Bank Restructuring Agency (IBRA) in May 2001.⁸⁷

- After much delay, APP at the end of January 2002 presented preliminary debt restructuring proposals for its Indonesian subsidiaries to the umbrella steering committee. APP promised to repay its debt over a period of 13 years, if all creditors would agree to a reduction of around 50% of the debt owed by APP's Indonesian subsidiaries. The proposals were instantly rejected by most of the creditors.⁸⁸

- In May 2002, the creditors' umbrella steering committee put forward its own proposals concerning the debt restructuring. This plan included measures such as the conversion of debt into equity and a proposal for the Widjaja family to make some form of contribution to APP. The company accepted some elements of the plan, but didn't endorse it fully. The umbrella steering committee was very disappointed by this response, according to a statement issued by ABN AMRO Bank (The Netherlands) on behalf of the committee.⁸⁹

- Angered by the slow progress in the debt restructuring process, two of APP's main financial creditors in June 2002 petitioned the Singapore High Court to appoint an independent management. The two banks which went to court were **Deutsche Bank** and BNP Paribas (France), which are owed US\$ 193 million and US\$ 20 million respectively. They were afraid the private creditors might lose out to Indonesia's government during the debt restructuring process. The two banks later won support of a number of other creditors.⁹⁰

- In a clear response to the court case pursued by part of the creditors, the Indonesian Bank Restructuring Agency (IBRA) threatened to unilaterally recover its US\$ 1 billion debt from APP. Despite the debt-standstill, IBRA secured a US\$ 90 million debt repayment by APP in June 2002.⁹¹

- At the end of August 2002, the Singapore High Court ruled against the petition of Deutsche Bank and BNP Paribas to appoint independent judicial managers for APP. Problems would increase by such a move, the court argued, as APP is incorporated in Singapore as a holding company and the judi-

cial managers therefore would find it difficult to restructure the group's units in Indonesia and China. But the court also warned that the outcome of a second petition may not be so favourable for APP if debt restructuring efforts were stalled again.⁹²

- The export credit agencies from Germany (**Hermes Kreditversicherung**), Japan, and the U.S. decided to team up with IBRA in July 2002. They signed an agreement which gave IBRA the task to reach a debt restructuring with APP by the end of September 2002.⁹³

- At the end of September 2002 APP finalised a framework outlining the debt restructuring plan for the US\$ 6.6 billion of debt owed by its Indonesian subsidiaries, including Indah Kiat. The plan was accepted by IBRA, the export credit agencies of Germany (**Hermes Kreditversicherung**), Austria, Canada, Spain, Sweden, Italy, France, Denmark and Finland, and Nippon Export and Investment Insurance (Japan). Under the agreement US\$ 1.2 billion will be paid back in full with interest over 10 years, US\$ 3 billion will only receive interest for 10 years after which a refinancing can be arranged and US\$ 2.4 billion will be rolled into a convertible bond.⁹⁴

- Other APP creditors, especially its bondholders, criticised the debt restructuring plan as it did not provide enough guarantees in the case APP would default again, and because the deal is signed before the debt restructurings of APP's Chinese operations (US\$ 2 billion) and of the holding company itself (US\$ 4.5 billion) have been finalized. Despite these criticisms, IBRA and 29 other creditors (representing 52 per cent of the debts of APP's Indonesian subsidiaries) signed a deal with APP in December 2002. Hermes Kreditversicherung and the other foreign ECAs did not sign, because key requests to be included in the restructuring plan were not yet addressed. The ECAs and the other creditors were given until 31 March 2003 to join the deal, else it would be concluded without them.⁹⁵

- Deutsche Bank and BNP Paribas (France) in January 2003 appealed the August 2002 decision by Singapore's High Court rejecting their application to have the management of Asia Pulp replaced. The first hearing is scheduled for mid-March 2003.⁹⁶

- In February 2003 a group of 11 foreign export credit agencies – including the US Exim Bank and the European, Japanese and Canadian ECAs – proposed the establishment of a holding company called APP Trading and an equity trust to hold the majority of APP's four Indonesian operating companies' shares until the full debt is repaid. The ECAs, which are owed about US\$ 960 million by APP, are only prepared to sign IBRA's debt restructuring plan when these conditions are met. APP and IBRA are opposing the proposal. The hope that the debt restructuring of APP could be finished after two years of negotiations, is now quickly vanishing.⁹⁷

Fibre supply

APP has fed its Indah Kiat pulp mills in Riau by clearing 287,000 hectares of natural forests over the past 12 years. That is about one third of all forests logged by pulp and paper companies in Indonesia.⁹⁸

The main supplier of pulpwood to Indah Kiat is PT Arara Abadi, an independent company also belonging to the Sinar Mas Group. Arara Abadi holds concessions with a total area of 300,000 hectares in Riau, part of which were part of the Tesso Nilo Forest only a few years ago. From 1997 to 2000, Arara Abadi supplied 72% of Indah Kiat's total wood purchases, mainly by logging the natural forests in its concession areas.

The remaining 28% were sourced from various other suppliers. This wood came primarily from land cleared for agricultural purposes by villagers, resettlements, the state forestry enterprise Inhutani IV and large-scale palm oil, rubber and other agricultural plantations with conversion permits.⁹⁹

Indah Kiat has been constantly back shifting predictions of the year by which it will source all of its fiber from pulp wood plantations. It now maintains that to be the case in 2007. Only around 20% of Indah Kiat's fiber needs were sourced from plantations in 1999. An independent study by a Singapore brokerage house indicated that Indah Kiat will source no more than 50% of the company's timber needs from plantations by 2005. But planting levels dropped substantially in 1998 and 1999, so the plantation fiber percentage may actually drop to around 30% in 2007, in spite of the 100% target set by the company for 2007.¹⁰⁰ In November 2001, an independent, preliminary supply assessment commissioned by APP concluded that much higher planting rates than presently realised were necessary to accomplish the targeted shift to plantation wood in 2007.¹⁰¹

Even when planting rates are increased Indah Kiat will find it very difficult to source its total hardwood requirements from the Arara Abadi plantation area, which has a net plantable area of 178,000 hectares. Additionally, the Sinar Mas Group has also taken steps to develop 25,000 hectares of additional areas through joint ventures with local cooperatives. Total plantable area therefore is 203,000 hectares.¹⁰²

An annual production of 1.8 million tonnes of pulp will need 9.0 million m³ of plantation wood. Acacia yields in the Arara Abadi plantation area are estimated to reach 175 to 200 m³ per hectare and presumably a eight year rotation period is used. Using these parameters, one can estimate that the Arara Abadi plantation area (including joint venture areas) will have a maximum annual yield of between 4.4 and 5.1 million m³, which is between 48 and 56% of Indah Kiat's annual fibre need.¹⁰³

While Arara Abadi's plantation yield is insufficient to sustain Indah Kiat's annual fibre need, several sources estimate that Arara Abadi's legal supply of timber from natural forests is also nearly exhausted. Indah Kiat will therefore have no other alternative than to purchase timber elsewhere, probably contributing to further deforestation of tropical forests in Indonesia.¹⁰⁴

The operations of Arara Abadi have raised other criticism also over the past five years. In 1997, Arara Abadi was one of the 176 companies in Indonesia identified by the Forestry Department, whose concessions had been affected by fire. Because they reportedly failed to submit proofs that they had not started fires in their concession area, their wood use license was temporarily suspended.¹⁰⁵

Large parts of the forestry concessions held by Arara Abadi traditionally belongs to the local Sakai people. There have been several reports on conflicts between Arara Abadi and the Sakai over the destruction of forest gardens, sacred places and burial places.

There have been several clashes between employees of Arara Abadi and villagers of the Betung village (Pangkalankuras subdistrict) trying to protect their land. In February 2001 the villagers of Betung were attacked by 700 employees of Arara Abadi. At least five villagers were injured in the attack, two seriously.¹⁰⁶

In January 2003, New York-based Human Rights Watch Asia released a report accusing Arara Abadi to be a “complicit in human rights abuses,” including having knowledge of attacks against villagers by security forces and militant groups in Sumatra over the past two years. The locals were protesting the logging by Arara Abadi of land which they believe was unlawfully taken from them under the government of former President Suharto.¹⁰⁷

NGO campaigns

An international coalition of NGOs including Walhi (Indonesia), Friends of the Earth and WWF has been exposing APP's Indonesian operations over the past few years. As a consequence of this NGO pressure, APP in June 2002 commissioned an extensive environmental and wood supply assessment by the independent consultants AMEC Forest Industry Consulting and APSE. The assessment will include “a multi-stakeholder dialogue to develop real solutions to issues identified in the assessment process” and should result in the completion of a 12-year Sustainable Wood Supply Plan for Sinar Mas operations in Sumatra.¹⁰⁸

APP promised the reports of this study would be available by the end of 2002. Yet, by the time of writing, March 2003, much of the necessary fieldwork has not even begun. At the same time, APP teams are clearing natural forest for new plantations every day.

Paper links between Tesso Nilo and Europe

Between 1997 and 2001, the total value of Indonesia's paper and paper product exports world-wide increased from US\$ 938 million to US\$ 2,034 million, a 117% increase. The total export volume for paper in 2001 was 3.2 million tonnes.¹⁰⁹

The Annex 1 lists the top five EU countries as importers of Indonesian pulp and paper, for the period 1999 – 2001. The second table in the Annex specifies the type of product imported by Germany. EU figures show a remarkable increase in 2001 as compared to the previous years. Also striking is Italy's top position, especially in pulp imports (32% of EU imports).

Web sites of many European paper factories have sections explaining how they deal with environmental issues in their production process. The companies are apparently very keen on showing a green image. However the sites visited for this survey did not indicate where the raw material comes from or how it is produced. Transparency appears to be limited. A special case is UPM-Kymmene (see paragraph on Finland).

United Kingdom

Investigations by Friends of the Earth (FoE) have shown that in the UK few paper products are sold that are branded as APP products. Instead the focus is on selling un-branded paper to UK agents and distributors, rather than on selling under those companies' own brands. It appears that both the re-branded products and un-branded products sourced from APP do not even have country of origin labels. Using indirect marketing distribution ensures that the origin of the paper is "unknown".¹¹⁰

An analysis of Indonesian pulp and paper exports to the UK by weight and value shows that there has been a significant increase in recent years. Between 1995 and 1999, pulp and paper imports into the UK rose from approximately 10,000 tonnes to 117,000 tonnes (see Annex). In sourcing their raw material by clear cutting rainforest and

avoiding the costs of setting up sustainable plantations, APP and APRIL are able to provide their paper at very low cost and significantly undercut many of their competitors.

While it is extremely difficult to identify all the paper products in the UK made from APP paper, in-depth research by FoE has identified the following companies as being involved in the import of APP paper into the UK. FoE points out that the extent to which any of them are aware of APP's social and environmental record is not clear.

- Robert Horne
- Spicers
- Kingsfield Heath

It is estimated that given the size of these distributors and the buyers groups that they feed in to, over 50% of the stationary wholesale supply business is contaminated with Indonesian paper from Asia Pulp & Paper.¹¹¹

Germany

Among the importing EU countries of Indonesian pulp, Germany ranks 5th, with 27,000 tons in 2001, and for paper it is not in the top five (see Annex 1).

Hamburg-based Papier Union GmbH is a subsidiary of Inapa Group, which is based in Lisbonne, Portugal. Papier Union sells 460,000 tonnes of paper annually, of which 110,000 tonnes consists of office papers (DIN A4). 15,000 tonnes of these office papers are bought in Indonesia, exclusively from APRIL. This concerns only the brand "Paper One", which, according to APRIL, is made purely from acacia pulp.¹¹²

Karstadt, the EU's largest department store chain used to carry APP paper until 2002, when they reacted to a pressure campaign by Hamburg-based Robin Wood and decided to no longer source from the Indonesian paper market.¹¹³

Finland

Finland's UPM-Kymmene has close ties with RAPP via APRIL. UPM-Kymmene is one of the leading paper companies in the world, with production facilities in 17 countries and a turnover in 2001 of nearly 10 billion euros.

UPM states that environmental protection and management are an integral part of its activities, and that it 'observes the principles of sustainable development'. An important objective in its choice of raw materials, sources of energy, production processes and in product development is to minimise the impacts on nature and the environment. UPM is listed in the Dow Jones Sustainability Index (DJSI) that represents the top 10% of the leading sustainability companies in the 33 countries covered by the biggest 2500 companies in the Dow Jones Global Index.¹¹⁴

In September 1997, UPM-Kymmene and APRIL announced an alliance for the production and marketing of fine paper products. The alliance was to establish two new companies: (1) UPM-Kymmene Fine Paper, consisting of UPM-Kymmene's paper mills, Kymi in Finland and Nordland Papier in Germany, and (2) APRIL Fine paper, consisting of paper mills in Riau and Changshu, China. The original plan was never accomplished as announced officially in September 1999. After this there has been no cooperation between UPM-Kymmene and APRIL regarding marketing or manufacturing. The companies have financial relations. In April 2002, they signed an agreement to extend until 2006 the USD 121 million loan UPM-Kymmene had granted APRIL in 1999.¹¹⁵

RAPP shares will remain as collateral for the loan. In connection with the loan extension, a series of environmental improvements regarding RAPP's pulp supply have been agreed on; they include a third party audit concerning illegal logging allegations and certifying concessions and mills according to ISO 14001 standards. UPM-Kymmene also expressed its support for the Tesso Nilo protected area projects.¹¹⁶

In August 2000, UPM-Kymmene bought APRIL's share of the Changshu fine paper mill in China, making it the sole owner. Simultaneously, the companies agreed that APRIL's Riau pulp mill, RAPP, would provide the Changshu mill with 200 000 tonnes of pulp annually for the next six and a half years. This makes UPM-Kymmene the

biggest single customer of RAPP. UPM-Kymmene is currently working with WWF to encourage their supplier RAPP to establish operational procedures that are based on sustainable wood supplies.

Netherlands

On the web site of the Indonesian National Agency for Export Development, four Dutch companies are listed as importers of Indonesian paper¹¹⁷:

- Kappa Graphic Board (Sappemeer)
- Timboost BVBA (Netherlands Antilles)
- Transibex International bv (Netherlands Antilles)
- Verhoeven bv (Arnhem)

Kappa Graphic produces 300,000 tonnes of graphic board annually, from 100% waste paper. It is unclear why this company is listed on the NAFED web site as importer of Indonesian paper.¹¹⁸

4.2.2 Oil palm companies

Riau's rapid land use changes in recent years are mainly due to the expansion of oil palm plantations, either by converting natural forest or change over from smallholder rubber holdings. Riau now has more land covered by oil palm than any other province in Indonesia. This growth has frequently led to social unrest, when after the fall of Suharto villages tried to reclaim land appropriated by large oil palm companies. In recent years, some companies tried to obtain village land by intimidating the local population or they have crossed the limits of their legal concessions ending up trespassing onto village lands.¹¹⁹ Land disputes have thus become common.

On the other hand, many villages have become interested in converting forest or rubber holdings into cooperative smallholder oil palm land. This is driven by a multitude of factors. Villages prefer regular income through oil palm but usually do not have the money to pay for the development. They are looking for investors and offer timber often without harvesting license as in-

centive. There appear to be plenty of investors looking for such opportunities. Some are interested in selling individual oil palm plots once the plants are harvestable at ca. 3 years of age to yet other investors who then integrate them into larger holdings. Others are only interested in the timber part of the deal and disappear before they have paid for the development of the freshly cleared forest land with oil palm.

As shown on the map in figure 3, the main oil palm companies with concessions in the vicinity of the Tesso Nilo forest are :

- Mitra Unggul Pusaka, owned by RGM group (Raja Garuda Mas)
- Surya Bratasena, owners unknown
- Musim Mas, owned by the Musim Mas Group
- Inti Indosawit Subur, owned by RGM and Salim Group
- Wana Jingga Timur, owned by the Darmex / Surya Darmadi Group
- Suntura Gajapati, owners unknown
- Warnasari Nusantara, owned by RGM group

Inti Indosawit is the main oil palm company active in the Tesso Nilo area, with a total of 130,000 ha as plantations in 1998.¹²¹ No research reports are available on the financial links of other companies.

PT Wana Jingga Timur, an affiliated firm of PT DPN (Duta Palma Nusantara) is in conflict with a local community. People are claiming land from the plantation area and demand that the company give them ownership rights as a compensation.¹²²

4.2.3 Timber companies

The third sector with concessions directly in the Tesso Nilo forest is the timber industry. This sector always arrives first and begins the long cycle of land use change. The first round of logging began several decades ago when very high value tree species were selectively cut for export as round logs. The second round was and still is the more saturating cutting of species with lower

COMPANY PROFILE

Inti Indosawit Subur¹²⁰

Ownership

PT Inti Indosawit Subur is owned jointly by two of Indonesia's largest corporations : Raja Garuda Mas and the Salim Group. Salim Group was Indonesia's largest until the financial crisis in 1997, which it managed to survive by considerable downgrading. Their joint-venture operated 108,000 hectares of oil palm plantations and 13 CPO-mills in Sumatra in 1997. Inti Indosawit falls under PT Asian Agri Plantation, the plantation flagship of RGM, which describes itself as the world's leading integrated palm oil producer with 200,000 ha of plantations in Sumatra and Kalimantan. In 2002, RGM sold large Indosawit holdings in Riau to a Malaysian group. RGM also owns RAPP, the pulp and plantation company discussed in the previous section.

Foreign financial involvement

As far as foreign financiers are concerned, Inti Indosawit mainly has relations with Fortis bank from the Netherlands :

- a Fortis subsidiary (Mees Pierson Trust) manages two financing companies in The Netherlands owned by Inti Indosawit (Asian Agro Int'l and Into Indosawit Int'l), in order to reduce tax payments on international loans.
- In 1997, \$ 300 million in bonds were issued to the Swiss bank UBS. Van Gelder (2001) considers UBS' influence on the company as 'strong'. The bonds are due in 2003.

value, for furniture and plywood but also round log export.

Some 80% of the Tesso Nilo forest complex continues to be managed by the logging companies Siak Raya Timber, Hutani Sola Lestari, Nanjak Makmur and the state-owned company Inhutani IV. Some 20% of the area is nominated to be cleared for the development of pulp plantations, mostly by Siak Raya companies. Several logging licenses were renewed at the end of

2000 just before new laws on timber concessions were about to go in effect and just when permit issuing government officials were “rotating” out of their positions.

Figure 2 shows timber concessions in and around the proposed Tesso Nilo conservation area, with a considerable overlap between timber (HPH) and especially pulpwood (HTI) concessions.

Several other concessions directly border the proposed area. These are owned by Wira Karya Sakti, Peranap Timber, Dwi Marta (now Inhutani) and Brata Jaya Utama. Hutani Sola Lestari and Nanjak Makmur appear to have connections to the Raja Garuda Mas group.

Siak Raya

Siak Raya Timber plans to deforest the northern part of Tesso Nilo. The company is part of KEA Industries in Singapore and has concession rights to selectively log and clear-cut forests for acacia plantations. Together with Inhutani IV in the East, the forest area of Siak Raya Timber represents some of the best elephant habitat in Tesso Nilo. The company manages a sawmill and a plywood mill in Riau where meranti, bitangor, kempas and balau are processed. Research by WWF Riau has shown that Siak Raya Timber buys logs from logging gangs. Siak Raya's mill also supplies plywood to the EU market.¹²³

Inhutani IV

Inhutani IV plays an important role in Indonesian forestry since, being state-owned, it can assume managerial authority over logged-over and abandoned concessions, and undertake reforestation. As a result of the national financial crisis in 1997-98, many timber companies have been forced into a partnership with companies of the Inhutani group. In Riau, there have been complaints that Inhutani IV has done very little on reforestation and was simply holding large areas of forest, generating resentment among local communities. Many Inhutani concessions do not seem to be under any form of control, and have been entered by illegal loggers or

leased to pulp companies for clearing, something which falls outside Inhutani's mandate.¹²⁴ There have been numerous cases of illegal log extraction by community groups on the Inhutani concession, especially going after high-value species such as balau, kempas and meranti to be sold to sawmills.¹²⁵ The two largest clear-cuts inside the Inhutani IV concessions have been organized by the Riau Landgrant College and the Air Hitam community.

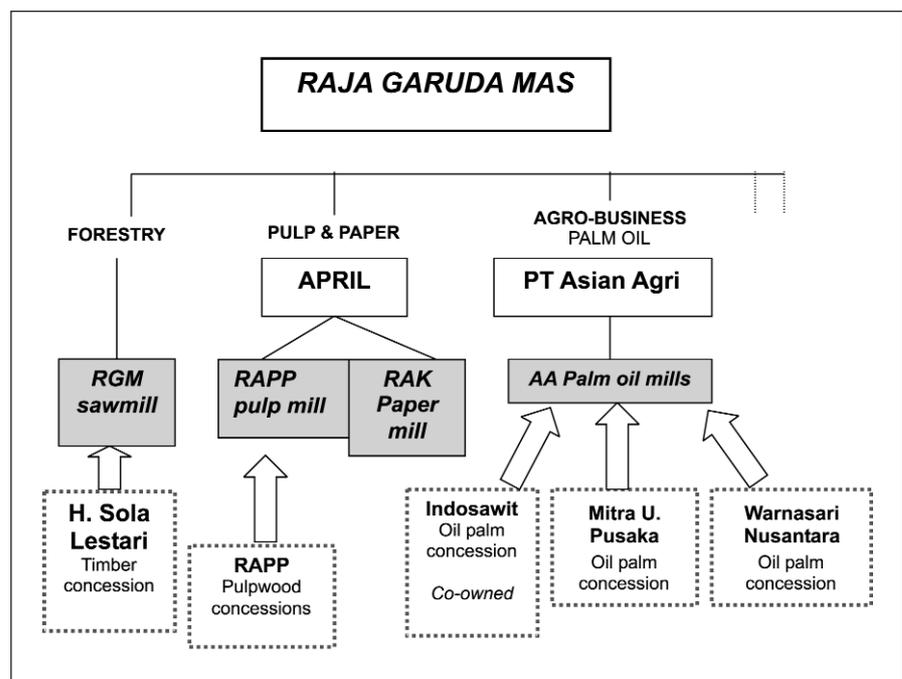
Inhutani IV admitted that they lack the capacity to control the concession adequately, and offered to hand over the former Dwi Marta concession to WWF.¹²⁶ In September 2002, the Ministry of Forestry suggested that this concession could form the first stage of a Tesso Nilo Protected Area.

4.2.4 Links between sectors and companies

Figure 8 shows companies active in different sectors in the Tesso Nilo area, that belong to one of the most dominant conglomerates, Raja Garuda Mas. Note that this is a simplified scheme, omitting several other RGM businesses and several intermediate levels; for instance, PT Asian Agri is the overall holding company for the oil palm sector, which includes many other companies and intermediates across Indonesia.

Regarding the other concession companies, no evidence was found of similar cross-sectoral links within the same conglomerate.

Figure 8. Companies active in different sectors in the Tesso Nilo area, belonging to Raja Garuda Mas.



5. WWF's position and actions

WWF's Asian Rhino and Elephant Action Strategy (AREAS) grew out of the recognition that conservation success for these endangered large mammal species will only be possible through a landscape-based approach that goes beyond isolated protected areas and includes the surrounding landscapes and related land-use practices. The AREAS program brings together conservation biology with trade monitoring, socioeconomic analysis, land use planning, and policy advocacy. AREAS works in nine priority landscapes across South and Southeast Asia and Indochina. Tesso Nilo in Riau, Sumatra, Indonesia is one of them.

WWF calls on the government of Indonesia to set aside Tesso Nilo as a protected area. Tesso Nilo is one of the largest remaining blocks of Sumatran lowland forest and has one of the world's highest plant diversities. Previous calls for its protection remained unanswered and this forest block has lost over 300,000 ha (62%) since 1985. WWF, and a wide range of partners, will try to integrate Tesso Nilo into a network of existing protected areas so elephants and tigers can move long distances and form large, viable populations. The ca. 3 million ha Tesso Nilo Conservation Landscape would secure ca. 600,000 ha of natural forests among a kaleidoscope of plantations, agriculture, settlements and infrastructure.

All of Riau's protected areas and the forests that connect them remain vulnerable to the pressures of development across Riau province. Therefore WWF calls on all companies who manage forests in Riau, their investors, creditors and customers

- a) to support the creation of the Tesso Nilo protected area,
- b) to protect all remaining High Conservation Value Forests in the province, and
- c) to act immediately to restore the balance between forest conservation and development across Riau.

The remaining High Conservation Value Forests will need to be secured, maintained and/or restored by stabilising the conversion frontier, and by mak-

ing both industrial and community land use practices in adjacent lands more compatible with the conservation needs of the forests.

In 2000, WWF began promoting the Tesso Nilo Conservation Landscape in a complex matrix of negotiations with communities; government at all levels; and several logging, pulp-and-paper, and oil palm companies, and their investors and customers around the globe. Everyone has a stake in this landscape. The task is to arrive together at an economically, socially, and environmentally sustainable land use plan that will determine the future of this area and everyone living there.

A few highlights of these negotiations include the expressed willingness:

- of APRIL and APP to not convert any more Tesso Nilo forest, stop purchasing wood illegally cut in the forest, support the declaration of a Tesso Nilo Protected Area, help secure the proposed protected area along a common border, and identify high conservation value forests in their concessions.

APRIL has followed up with some very concrete steps on the ground. But much more needs to be done, especially by APP:

- of the Government of Indonesia to convert its logging concession Inhutani IV into the first part of the proposed Tesso Nilo National Park, and processing of the necessary paper work.

- of the logging companies who hold concessions for the remainder of the Tesso Nilo Forest to negotiate which parts of their concessions could immediately be transferred into the proposed park and what would happen then to the rest.

- of communities bordering the Tesso Nilo forest to negotiate ways that would make them stop illegal logging in the forest in return for fair access to the province's economic market place and for insurances that outsiders are prevented from illegal logging also.

In 2002, the Critical Ecosystems Partnership Fund (CEPF) selected the Tesso Nilo Conservation Landscape as one of four Sumatran conservation

hotspots to focus on. CEPF began supporting NGOs in their work to protect the landscape. WWF is now part of an alliance of 24 local and national NGOs working on the social, ecological, policy, and economical issues that will determine the survival of the landscape's remaining natural forests.

Since 1999, WWF Indonesia's work in Riau and on the national and global issues connected to it has been supported by the Critical Ecosystems Partnership Fund, Nancy Abraham, Rumbai Ecology Club, Sall Family Foundation, US Fish and Wildlife Service, WWF Germany, WWF Japan, WWF Netherlands, WWF Switzerland and WWF US.

WWF calls on these main players to work together to save Tesso Nilo and other high conservation value forests:

- **The Indonesian Government** should declare the whole Tesso Nilo forest as a protected area and ensure that it is effectively managed. The Government of Indonesia should help create wildlife corridors to link Tesso Nilo to other existing protected areas and ensure their full protection. The Government of Indonesia should develop, communicate, and enforce a clear policy that protects all high conservation value forests. WWF is prepared to help develop that policy and provide tools for the identification of high conservation value forests.

- **Riau's provincial and district governments** should review land-use plans to prevent further conversion of high conservation value forests and ensure that the province's natural resources are developed sustainably. WWF is prepared to help develop new or re-design existing land use plans in partnership with government authorities and other stakeholders.

- **Riau's pulp and paper industry** should protect the High Conservation Value Forests within their concessions and those of all their suppliers, operate within the limits of clearly defined legal and environmentally and socially sustainable wood supply plans, and ensure sound forest stewardship in plantations from which they source fibre for paper.

WWF is prepared to work with the industry to develop the relevant management practices.

- **Financial Institutions and Banks who invest in the pulp and paper industry in this region** should ensure that their investments are not being used to support the conversion of forests of high conservation value or the violation of traditional land rights. WWF is prepared to assist financial institutions and banks to develop their investment policy and criteria for forest industries and to advise on future investments in the sector.

- **Customers of products from this region** should ask for environmentally sustainable manufacturing processes so their purchases do not lead to the destruction of more natural forest and the deaths of elephants and other wildlife. WWF is prepared to advise companies in the development of sustainable procurement policies.

6. Recommendations by this study

This study, which brought together and synthesised the findings and insights obtained in recent years by various experts and organisations, confirms clearly that the next few years will be critical in preventing complete deforestation of the Tesso Nilo Forest and other natural forest blocks remaining in the Tesso Nilo Conservation Landscape. Land use decisions in the province are influenced by a complex web of public and private entities operating at local, provincial, national and international levels. It is up to conservation organizations to seek to influence decision making at any of the above levels. No single organization will be strong enough to advocate the protection and sustainable use of resources that are in such high demand by government, industry and the general public. At a time when natural forest resources have become so rare that the few remaining blocks draw the interest of all the major players in this game, only a strong alliance of local, national and international conservation organizations is likely to stand a chance to influence the scene.

Particular attention is to be given to identifying potential early adopters of sustainability policies and practices from the non-conservation sector that have the clout and credibility to generate a critical mass within their own economic and governmental sectors, at different positions in the trade chains. Successful campaign work by WWF and FoE has generated initial momentum that is to be expanded. They play a crucial role in the so-called mainstreaming process, which starts with the development and subsequent adoption of practices that comply with ecological, social, institutional and economic sustainability criteria. The early adopters within each sector are the ones that should convince the mainstream to follow their example. This mainstreaming process can be facilitated and accelerated by the development of incentives and the removal of disincentives, in which governments, international financial agencies, donors and NGOs are key players.

Local communities are a target group in their own right, which require a socially sensitive approach. They can

be both opponents and supporters of conservation programs, depending on whether their immediate and longer-term interests are at stake, whether their land rights are recognised and secure or being threatened or denied, and on a combination of awareness raising, introduction to successes elsewhere and concrete incentives.

The following recommendations by AIDEnvironment are complementary to the numerous actions and initiatives that WWF, other NGOs and parts of the private sector have taken already to save Tesso Nilo and other forests in Riau. These have been presented in other chapters in this report. Some of the recommendations below are currently being discussed by the NGOs active in Riau; in that case, their mentioning here is meant as encouragement.

Overall recommendation

- In view of the urgency of the situation in Tesso Nilo, the private sector has to contribute to reduce its pressure on this area. Therefore, it is essential that the multi-stakeholder process involving the private sector, government and NGOs gains force and momentum. It might be necessary that the key market actor representatives at one point in the not too distant future come together to make commitments – otherwise the “prisoner dilemma” will make it impossible for each actor to move forward. Vigorous campaigning by NGOs and by consumers of products that may have been produced in the Tesso Nilo region must maintain the necessary pressure.

Recommendations to Governments

- The Indonesian Government, from national to local levels, can and should create an enabling environment by removing negative and applying positive incentives towards sustainable land use. Examples are the elimination of incentives for further pulp & paper capacity expansion in Indonesia (tax incentives, wood supply subsidies), adoption of development policies that are based on sustainable supply planning to prevent over-capacity in the first place, and introduction of certificates of legal origin plus a corresponding tracking system.

- Similarly, governments of consumer countries can and should create an enabling environment by removing negative and applying positive incentives towards sustainable industry and trade practices. Examples are favourable import tariffs for imported certified products, transparency legislation (see below) and a ban on imports of illegally sourced timber.

- Indonesia and consumer countries should enact legislation on transparency requirements for business corporations: investments, trade in forest products (e.g. timber, pulp, paper, palmoil), chain-of-custody tracking and practices by (Western) companies in Indonesia.

- The Government of Riau should effectively implement and monitor a new provincial land use plan that meets sustainability criteria (it is not sufficient that WWF is invited to help prepare one).

- A trust fund and/or a public-private foundation should be established to ensure the necessary long-term financial sustainability needed to cover the costs of managing and protecting the Tesso Nilo protected area and the surrounding landscape. The fund could be capitalised with contributions from donors that are directly, indirectly or not linked to Riau province, and could possibly include contributions from debt-for-nature swaps.

- Indonesian government agencies at all levels are likely to remain weak for some time to come. Therefore, ‘good governance’ donor programs can help strengthen provincial and local government institutions, including support to a credible anti-corruption offensive. Curbing illegal logging should be a priority goal in such programs.

- Any development strategy or financial support from governments of consumer countries should be integrated with such good governance programs.

- Any development strategy involving local industries and their respective global business partners would need to be integrated with local government and community concerns. Education programs, conservation-compatible development projects and special incentives (e.g. compensations based on op-

portunity costs, support in securing justified land claims) would need to be considered.

- An independent monitoring / watchdog structure should be established, similar to the role the NGO “Global Witness” plays in Cameroon and Cambodia after agreements between the respective governments and the World Bank were reached.

Recommendations to the Private Sector

Corporations which lobby Indonesian authorities to obtain permits to convert large stretches of natural forest to plantation crops pose the highest threat to the Tesso Nilo landscape. The larger these companies are the more likely it is that they are linked to the web of the global economy. They need to make money, either from investors or from customers. Both are likely to include international partners. Some of these potential or existing international business partners may view it unfavourably to be associated with a supplier who converts some of the last remaining tropical forests in Sumatra. These partners may be able to influence the company operating in Riau.

International campaign work may be able to attract companies that are willing to engage in strategic conservation partnerships designed to bring about sustainable operations of the Indonesian suppliers. Should these partnerships show positive results in their operations other companies might be convinced to follow the example thus creating a critical mass that might drive conservation thinking in the whole province.

- Logging concessionaires should adopt sustainable forest management and certain conservation principles, e.g. to refrain from logging high conservation value forest areas by setting them aside as conservation zones within their concessions.

- Corporations should be willing to agree on fair take-overs of concessions with high biodiversity values by a conservation organisation that transfers the area to a local management structure.

- Corporations should be willing to develop and apply best practices for

Early international adopters in sustainable palm oil

- The Migros supermarket chain in Switzerland has committed itself in 2002 to buy only palm oil from ecologically sound and socially acceptable sources (that e.g. exclude plantations on converted forest land). Migros has begun working with certified sources in Ghana.

- In 2002, four Dutch banks have committed to stop or substantially restrict financing oil palm development in Indonesia if this has been preceded by the conversion of natural forest.

their sector, and apply transparency rules in their entire production or investment chain (origin of their raw materials or imported goods, chain-of-custody tracking, independently verifiable impact assessment reports etc.).

- All corporations in the supply chain for timber, pulp & paper and palm oil should join WWF's efforts to evaluate the conservation value of the forests which would be converted, and ask their suppliers to respect the evaluation and to not convert high conservation value forests. A temporary moratorium on forest conversion should be put into place until all forests have been evaluated.

Recommendations to Investors and Financial Institutions

As this and other reports have made clear, the expansion of Indonesia's plantation industry requires large amounts of capital. The role and responsibility of financial institutions is therefore of particular importance, as they provide the credits, equity and other financial services that plantation companies require to open and expand their estates. Financial institutions that are substantially involved in providing this capital must assume their responsibility and, therefore, be prepared to influence the environmental policies of their clients.

- Loans granted by investors, financial institutions and export credit agencies should be based on clear environ-

mental and social criteria and on related monitoring mechanisms to be complied by the timber, plantation and pulp and paper companies that are active outside in the broader Tesso Nilo landscape (WWF is in dialogue with HERMES, USExIm, Swedish ECAs).

- Investments and contributions should be made to a sustainable development trust fund that supports alternative livelihood options for local communities.

- Improved due diligence practices should be applied by financial institutions funding projects in the agro- or forestry sector (assessment of environmental risk, codes ensuring that funds are not used for illegal activities, independent audits).

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Annex 1

European Union imports of pulp and paper products from Indonesia 1999-2001

	Weight (1,000 tonne)			Import value (million US\$, cif, nominal)		
	1999	2000	2001	1999	2000	2001
Pulp:						
Italy	72	66	147	33	43	63
France	26	34	93	9	21	40
Netherlands	11	21	62	5	14	28
UK	18	28	43	8	18	21
Germany	24	29	27	11	20	11
Others	11	25	92	5	16	41
Paper:						
UK	99	79	55	70	65	50
Italy	62	38	37	45	33	29
Belgium	65	20	34	48	16	27
Spain	82	33	24	59	27	21
France	34	22	21	24	18	18
Others	9	36	46	12	35	44

German imports of pulp and paper products from Indonesia 1999-2001

	Weight (1,000 tonne)		
	1999	2000	2001
Pulp:			
Total	25	29	30
4702	1	0	6
4703	24	29	24
Paper:			
Total	1,4	4,8	4,9
Others	0,1	0,5	0,1
4810	0,0	1,7	0,1
4819	0,2	0,4	0,5
4820	0,7	1,3	1,1
4823	0,4	1,0	3,0

Legend:

- 4702 Chemical wood pulp, dissolving grades
- 4703 Chemical wood pulp, soda or sulphate bleached, non-dissolving grades
- 4810 Coated paper for writing/printing
- 4819 Packaging
- 4820 Books of stationery, exercise books, albums
- 4823 Other paper/paperboard (mainly for writing/printing)

Source: World Trade Atlas (monthly time series) (via Ed Matthew / James Hewitt, Friends of the Earth)

Annex 2 – Banks' responses

WWF asked the German banks and financial institutions presented in this study to comment on their relations with APP. Their responses are summarised in this Annex. WWF cannot accept responsibility for the correctness of these statements.

Commerzbank

1. Loans to Indah Kiat

Commerzbank has not been in credit relations with this company for more than a year.

2. Loans to APP group

We have severely cut back our credit involvement in recent years. Our present, very low credit risk is based exclusively on HERMES credit insurance.

3. Indah Kiat shares

CICM, our subsidiary, had some Indah Kiat shares in an index fund. The goal of such a fund is to reflect the performance of the basic market index. This reflection basically takes place without analytically evaluating the business in question. Here it is simply about representing the market index. The shares were sold in 2002. Now that we have sold Montgomery Asset Management, we naturally can't make any comments on that.

Dresdner Bank

We have carefully reviewed the statements in your study, especially those on whether the bank has business relations with the businesses in Indonesia and Singapore mentioned in the study. Out of the bank's duty to maintain confidentiality, we are prevented from giving information on the mentioned events or on the question of whether or not business relations exist with the companies named in the study. To bypass this legal hurdle, we are trying to obtain written permission to release information, freeing us from the bank's duty to maintain confidentiality, especially regarding those companies where no credit relations have existed for years. We are very interested in correcting the information cited in the study.

But in general we can note that in our last statement on the palm oil industry, we drew attention at that time to the framework conditions of our credit involvement. They include:

- As the first signatory to the UNEP Statement by Financial Institutions on the Environment and Sustainable Development, the Dresdner Bank pledged as long ago as 1992 to take environmental interests into consideration in all our business activities and to fulfil all regional, national, and international environmental requirements;
- Our environmental programme and environmental guidelines, which apply for our whole group, expressly prescribe

that environmental risks and factors be included in the credit risk investigation;

- Information for all customer advisors and specialists are set down in our in-house handbook, "Environmental Risks in Credit Transactions";
- Operatively, our guidelines for credit transactions abroad prescribe that the latent risk of environmental problems is also taken into consideration during the investigation of credit worthiness.

HVB Group

Financial backing extended by HVB Group to Indah Kiat, Asia Pulp & Paper or Sinar Mas Group is largely state-guaranteed loans for orders such as paper machines. The problem here is that the influence of banks on sustainability is very low when it comes to loans for orders because

- loans are often just for partial consignments in larger projects,
- banks are only called in at a very late stage and therefore see project details correspondingly late in the process,
- delivered products often don't have detrimental environmental impact (such as printing machines), and
- in most cases, state insurers guarantee the loans and therefore their environmental principles are decisive.

The last point has led us to call for the observation of World Bank standards by state credit insurers in relevant committees in all OECD member states. We have advocated this view, especially in the German government's Interministerieller Ausschuss (IMA) [inter-ministerial committee] and in the Association of German Banks, but we couldn't assert ourselves against the majority.

To do justice to this demand, HVG Group prescribes in its credit principles that the bank also orients its credit-granting facility on basic ethical values. In particular, this includes environmental protection and the observation of World Bank standards. Thus, the investigation of environmental risk is an integral component in investigating credit worthiness. The minimum standard for financing projects and orders is the observation of World Bank standards and all local, national and international laws. For us, these principles have already led several times to us turning down a request for credit. In view of these financing principles, requests today from Sinar Mas Group for credit would have been decided differently.

We would also like to point out that during debt restructuring negotiations between banks and state credit insurers with Sinar Mas Group, HVB Group has insisted that sustainable wood supplies from reforested areas are used in production and that Sinar Mas Group implements World Bank standards. Negotiations to restructure debt are based on cash flow planning that assumes the raw material costs of wood in the long term will be pegged to the market price of wood from such reforestation projects. These ongoing discussions with Sinar Mas Group have also led to the hiring of AMEX

Simons, an independent firm of experts on forest affairs, to develop a long-term wood and raw material plan for the future.

As a matter of principle, these syndicated loans are made public; in this respect, the names of the banks giving the syndicate credit and the borrower are available to everyone.

Norddeutsche Landesbank (Nord LB)

As a matter of principle we do not release information about our customers to third parties. But since you have explicitly named us as a reference in the draft of your "Tesso Nilo" study, we would like to tell you that we

1. have not issued any bonds for Indah Kiat Pulp & Paper,
2. have given only temporary, short-term loans to Indah Kiat Pulp & Paper,
3. have not provided any syndicated facilities to APP Group in the 1990s.

Nord LB has not had any business relations with Sinar Mas Group or group companies for some time.

Deutsche Bank

There aren't any objections regarding the study's contents as far as they have to do with the Deutsche Bank.

Union Investment

Indah Kiat – we don't carry shares in our portfolios any more. We sold our shares several months ago.

Baden-Württembergische Bank, a subsidiary of Baden-Württemberg Landesbank

Regarding your inquiry, we inform you that Robin Wood has already asked about Baden-Württembergische Bank involvement in Southeast Asia in a check of banks Robin Wood carried out on 13 February 2002. We were asked whether we have financial associations with the Southeast Asian oil palm and paper industry. At the time, we replied to Robin Wood that we do not offer financial services to the Indonesian oil palm or paper industry; rather, the bank's involvement in this region is limited to export financing in the interest of our customers, and to business with local banks. Thus, through our Hong Kong branch, we did in this case contribute a small amount to a syndicated loan for APP Paper Trading Pte Ltd, Singapore. The arrangers at that time were Bank Boston, Norddeutsche Landesbank, Development Bank of Singapore and KBC Bank.

The borrower was a sales subsidiary of APP Group. APP Group, listed on the New York Stock Exchange, also has production sites for manufacturing paper in Indonesia, China and India. Our credit was a structured loan and served only to pre-finance the export earnings of this APP Group subsidiary.

Annex 3 – Position papers



Forest Conversion

During the last twenty years of the twentieth century, 300 million hectares of tropical forests were converted to non-forest land-uses worldwide. The conversion of forests to other land uses imposes severe environmental and social costs due to the ecological impacts of clearance, uncontrolled burning, and disregard for the rights and interests of local or indigenous communities. Without significant changes in policy and practice, the process of forest conversion is likely to continue at a rapid rate and pose a major threat to High Conservation Value Forests (HCVF – see separate position paper), freshwater ecosystems, livelihoods of forest dependant peoples and habitats of endangered species such as elephants, rhinos, tigers and great apes. Reduction of wildlife habitat leads to increased human-wildlife interaction and conflict.

WWF defines forest conversion as a continuous process of forest degradation, leading from natural forests over one or several steps to the replacement of forests by other forms of land use, such as plantations, agriculture, pasture, mining and urbanization. The driving forces behind forest conversion vary and are often interrelated. Among the most important are: the fact that forests are not valued for the long-term benefits that they provide, and that conversion often costs very little money. This creates incentives to log and sell the valuable timber out of forests and then convert the degraded forest land to more profitable land uses rather than to undertake sustainable forest management. Non-existent or insufficient landscape planning procedures and lack of guarantee of land ownerships and tenure rights often set the ground for uncontrolled and unwanted forest conversion processes.

WWF believes that forests are amongst the most diverse and valuable ecosystems around the globe. They provide a wide range of products and benefits for humans and nature that can rarely be substituted through other means. Therefore in general every effort should be made to prevent any forest, but especially HCV Forests from, being converted. WWF recognizes that under certain conditions planned and targeted conversion can be beneficial or necessary to reach specific goals of public interest without endangering the overall functionality of forests. Where conversion is planned the following conditions shall be fulfilled:

- Identified High Conservation Value Forests should not be affected by any forest conversion
- At a minimum, conversion must not contribute in any way to the extinction of species, or to the loss of significant subpopulations of an endangered species
- The total forest cover within a country or region should not be below an agreed long-term goal described in a National Forest Programme or planning documents developed through a multi-stakeholder process
- There should be proven and agreed public interest and benefits from the new land-use, that surpasses public interest in forest conservation
- There should be a transparent planning process on a landscape level, involving all relevant stakeholders
- Independent environmental and social impact assessments should be conducted and the necessary measures to prevent negative impacts of the conversion implemented

WWF will work together with governments, public and private institutions and other partners towards the elimination of unplanned and damaging forms of conversion to safeguard biodiversity and social values by:

- Calling for transparent planning processes to achieve an optimal distribution of natural forests, plantations, agricultural areas, urban areas and other land-uses in a given landscape. This includes well-informed negotiations among a wide range of stakeholders to balance ecological, social and economic dimensions of natural resource use across the landscape
- Enforcing adequate safeguards that recognize and guarantee the legal and customary rights of indigenous peoples and rural population to own, use and manage their lands, territories, and resources
- Engaging with financial institutions and market actors in forest conservation and lobbying for the elimination of policy incentives that contribute to forest conversion and forest destruction



Position Paper

February 2002

One of a series of position papers produced as WWF's response to the WWF/IUCN Forests for Life strategy and WWF's current five-year target-driven programme on forests

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Oil palm

According to the WWF Living Planet Index, the tropical forest species index declined by 25% in the last thirty years. Worldwide, 300 million hectares of tropical forest were converted to non-forest land-uses during the last two decades of the twentieth century. Most of the world's oil palm plantations are within these converted hectares.

Oil palm plantations have often imposed environmental and social costs due to indiscriminate forest clearing, uncontrolled burning with related haze, and disregard for the rights and interests of local communities. Without significant changes in policy and practice, the expansion of oil palm plantations poses a major threat to high conservation value forests, freshwater ecosystems, livelihoods of forest dependant peoples and habitats of endangered species such as elephants, rhinos, tigers and orang-utans.

WWF recognizes that palm oil is a basic foodstuff with high consumer demand. The industry generates valuable foreign exchange earnings and employment opportunities for tropical producer countries. WWF is, however, deeply concerned at the prospect of the industry continuing to expand and operate in an unsustainable manner. WWF calls upon the industry, regulators, financiers, buyers and other stakeholders to work collectively to develop and promote adoption of environmentally appropriate, socially beneficial and economically viable practices in the oil palm industry.

WWF believes that key elements of sustainability within the oil palm industry are:

- **Maintenance of high conservation value forests:** Oil palm plantations should not replace high conservation value forests (see separate position paper). This will normally require well-informed negotiations among a wide range of stakeholders to achieve optimal integration of oil palm plantations with the mosaic of other land-uses in a given landscape or ecoregion.
- **Sound environmental management practices:** Industry participants should adopt management practices to minimize environmental impacts such as air and water pollution, forest fires, soil erosion, pest invasion, human/wildlife conflict and biodiversity loss.
- **Respect for rights of local communities and indigenous peoples:** Industry participants should recognise the legal and customary rights of local communities and indigenous peoples to own, use and manage their lands, territories, and resources. Plantation development should not proceed in areas over which there are unresolved tenure disputes.
- **Positive social impacts:** The industry should maintain or enhance the long-term social and economic well being of plantation workers and local communities. In many cases this will include the strengthening and diversification of the local economy to avoid dependence on a single plantation product.
- **Proficient regulatory frameworks:** Regulatory frameworks should encourage practices that will achieve the desired environmental, social and economic outcomes described above. At a minimum, industry participants shall respect all applicable laws of the country in which their plantations and mills are sited. However, responsible behaviour will often require standards of performance that exceed the requirements of local and national laws, especially where regulatory frameworks are underdeveloped or governance is weak.
- **Transparency:** Industry participants should adopt and make public their policies, practices and implementation plans pertaining to their social and environmental performance. They should encourage independent monitoring of their performance and make public their findings. They should involve local stakeholders both in the development of standards and performance monitoring.

WWF will work with governments, private companies, financial institutions and civil society organizations to:

- Develop and promote adoption of policies and practices consistent with this position
- Eliminate incentives for oil palm plantations to replace high conservation value forests



Position Paper

February 2002

One of a series explaining the WWF/IUCN Forests for Life strategy and WWF's current five-year target-driven programme on forests. For further details contact

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Illegal Logging and Forest Crime

Introduction

The global trade in illegally extracted timber is a multi-million dollar industry. Illegal logging: *occurs when timber is harvested, transported, processed, bought or sold in violation or circumvention of national or sub-national laws.* Although generally portrayed as a problem in tropical forests, illegality also occurs in developed countries and economies in transition. Even those countries that pride themselves on good domestic management are not exempt. Illegal activities have a particularly devastating impact on biodiversity because they often deliberately target remaining pristine forests, including protected areas, which contain the highly valuable hardwood species that have been logged out elsewhere. Forest crime also affects human communities through loss of natural forest resources and sometimes through intimidation and violence. The hundreds of millions of dollars of tax revenues lost around the world as a result of forest crime also has a wider social impact.

WWF believes that illegal logging and other forms of forest crime are part of a larger problem that includes issues of forest governance and corruption. They extend far beyond some individuals violating resource-management laws. WWF uses the term "illegal logging and forest crime" to include both large and small-scale timber theft and a variety of issues such as transfer pricing, breaching tax rules, any illegal aspects of timber sourcing and circumvention of concession agreements through bribery or deception. Poor governance and forest management can also lead to increased access to, and unsustainable utilisation of forests and an increase in activities such as illegal mining, bushmeat hunting and settlement. There is also a whole range of corrupt activities, which has the cumulative effect of reducing effectiveness of governance even if the precise letter of the law is not breached. Up to 65 per cent of WWF's Global 200 forested ecoregions are threatened by illegal logging. WWF believes that illegal logging and forest crime are best stopped using a combination of existing tools and the development of new policies:

WWF will work with partners, international organisations and governments to:



Position Paper

April 2002

One of a series of position papers produced as WWF's response to the WWF/IUCN Forests for Life strategy and WWF's current five-year target-driven programme on forests. For further details contact

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- Promote improved transparency and enforcement of existing laws. Where necessary encourage amendment or drafting of new legislation and strengthening of implementation
- Promote independent monitoring and auditing schemes such as that provided by the Forest Stewardship Council for forest management and tracking wood products from the forest to the end user
- Encourage consumer countries to provide aid and technical assistance to producer countries to address the root causes of forest crime (including poverty alleviation)
- Support Global Forest and Trade Networks linking buyers and consumers of certified forest products
- Work to build human resource and institutional capacity to plan and manage the forest estate (protected areas, production forests and community-managed forests)
- Assist the implementation of systems for the verification of legal compliance, especially in countries where certification will take some time to develop
- Promote and encourage the use of government public procurement to specify timber and wood products from legal and sustainably managed forests
- Support the adoption of voluntary bilateral trade agreements that ensure the supply of legal timber as a first step in applying responsible procurement policies

- Raise awareness of the social and economic impacts of illegal logging and forest crimes amongst key audiences: governments, business, industry and consumers
- Increase the use of CITES as a tool against timber-related crime
- Engage with financial institutions to ensure adequate forest policy safeguards are in place so that investments do not facilitate illegal logging and forest crime



WWF is the world's largest and most experienced independent conservation organization. It has 4.7 million regular supporters and global network active in 96 countries.

WWF's mission is to stop the degradation of the planet's natural environment and to build a future in which humans live in harmony with nature, by:

- conserving the world's biological diversity
- ensuring that the use of renewable natural resources is sustainable
- promoting the reduction of pollution and wasteful consumption.

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