

# FOREST AND LOG EXPORT MONITORING SYSTEM IN PAPUA NEW GUINEA

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Twelve years ago the Government of Papua New Guinea (through its agency the PNG Forest Authority) addressed the issue of illegal log export practices by appointing the internationally known Swiss inspection company SGS to develop and implement a monitoring system for all log exports from the Nation. The system (including modern log tracking technology) introduced by SGS has been very successful in enhancing revenues for the Nation and providing international credibility for the Government in demonstrating that this controversial sector is under control. The SGS system ties in closely with the existing PNGFA monitoring system to assure buyers that a reputable independent inspection company has verified that PNG logs have been exported in the quantity, quality, value (with taxes paid) and from the area as approved by Government. This is an important foundation for any future legal verification requirements which may include social and environmental factors as increasingly demanded by ENGOs. The adoption of such a legal verification system (on a voluntary basis) is being considered by the PNG Forest Industry Association.

## BACKGROUND

### The need for independent third-party monitoring

Although the processing industry is growing, forest product exports from Papua New Guinea are still dominated by raw logs. PNG exports 2 to 3 million m3 of logs each year with a total fob value of US\$150 to 200 million. A Royal Commission of Inquiry into Papua New Guinea forest sector in the late 1980's revealed widespread abuses in the forest industry - transfer pricing through mis-declaration of log cargoes and artificial pricing being particularly rampant. These abuses were costing both Government and landowners millions of dollars each year. The new Forestry Act of 1991, designed to address the problems identified by the Inquiry, also set up the Papua New Guinea Forest Authority (PNGFA). The Government recognised that it needed to act very quickly to halt losses to the Nation from export logging and accordingly tendered for a log export monitoring system to be implemented promptly.

The tender was won by a Swiss-based inspection company, SGS. By contracting this service out to a large international verification company such as SGS, the Government was allowing the PNGFA to concentrate on the vital role of monitoring forest operations at the cutting face. The contract was also to facilitate the introduction of new technology and management systems to PNG citizens.

Over 12 years of operation the SGS system has proven to be very cost effective in increasing revenues to both Government and traditional resource owners. Also the international credibility of the PNG forest sector has been considerably enhanced by the engagement of an independent and reputable company to verify log exports. This was an extremely controversial area prior to 1995 but since then the Government has gained international kudos for taking prompt and effective action to get this area of the economy under control.

This international credibility has also proven important for protecting PNG's overseas markets for

timber products. Due to ENGO pressure many overseas buyers and their Governments are moving to restrict or stop purchases of forest products from countries where logging is regarded as out of control. Increasingly it is becoming incumbent on the forest industry to prove the legal origins of its log sources to maintain offshore markets. With a system of independent log export monitoring already well established, PNG can assure overseas buyers that the logs have not come from smuggled sources and the country is well placed to build on this system in future to give additional proof of legality according to market requirements.

## GENERAL OVERVIEW OF VERIFICATION

### Party responsible for issuing verification

Verification of forestry operations in PNG are primarily the responsibility of the PNG Forest Authority who have contracted out the monitoring of export log shipments to SGS.

The PNGFA is responsible for granting permission to harvest logs, monitoring the actual forest operations and granting permission to export forest products. However, it is a fundamental point under PNG law that unalienated land (97% of PNG including all forest areas) are owned by the people who have traditionally lived on it for generations and development cannot occur without their permission. All logging companies must be registered as Forest Industry Participants with the PNGFA which first checks that they are legally registered with the Registrar of Companies under the Investment Promotion Authority.

Under the Forest Act 1991 (and amendments) the PNGFA issues a Timber Permit to a company only after an extensive 34 step process that begins with providing awareness to traditional landowners whose approval to enter into a Forest Management Agreement (FMA) is required before any further action. A company is issued with the Timber permit only after a lengthy consultation (at landowner, Provincial and National

Government level) and tender process. The Timber Permit stipulates all the operating conditions such as harvest/export/processing quotas, benefits to be provided, royalties, levies and other charges to be paid etc.

However, the bulk of PNG's existing forest concessions are operating under Permits that precede and are preserved by the 1991 Forest Act. These are generally operating through Timber Permits under Timber Rights Purchase Agreements that have been signed between the traditional landowners and Government or Local Forest Areas where Government has granted landowners the right to negotiate directly with logging companies. In most of these cases the Timber Permit or LFA is held directly by a landowner company who engage a contractor to operate the area under a Logging and Marketing Agreement. Large-scale Agriculture and Roadline Projects can also be granted permission to harvest and export logs under a Timber Authority (TA) Agreement.

All forest concessions in PNG are subject to planning monitoring and control regulations established by the PNGFA. These ensure that logging proceeds in an orderly fashion in accordance with the Timber Permit, that socially and environmentally sensitive areas are excluded from logging and that logging takes place in accordance with sound forest management and environmental practices. Monitoring is carried out by the 120 staff of the PNGFA Field Services Division. Most concessions have a PNGFA Project Officer based on site and are equipped to undertake monitoring operations.

PNGFA officers from the Marketing Section are also involved in the export process. They must approve the species, volume and prices proposed and issue an Export Permit (signed by the Minister) which shows all this information. A copy is also provided to SGS who are responsible for ensuring that the actual shipment follows these approved specifications. The Department of Trade and Industry also issue an Export Licence with the same information but only if the PNGFA approves. This appears to be a duplication but is a requirement of PNG law.

The PNGFA is also responsible for the licensing of log scalers. Companies are required to use licensed scalers who must follow regulations that apply to the measurement and declaration of logs in PNG. In general the requirement is that all operators must declare their monthly log production in a prescribed format which includes a summary of volumes extracted for each landowner plus the royalties owing to them.

The PNG log export monitoring service was developed and is run in conjunction with the PNGFA by Société Générale de Surveillance (SGS) of Geneva, Switzerland. The SGS group is the world's largest verification, testing and certification company. With its headquarters in Geneva and 48,000 staff world-wide, it operates a network of 1180 offices and 321 laboratories in 145 countries. The Forestry Monitoring Programme of SGS offers services to governments, companies and international institutions aimed at revenue protection, trade facilitation, legal and sustainable use of natural resources.

SGS PNG Limited was set up late in 1994 to develop and operate the monitoring system. Currently SGS PNG operates with a staff of 40 (including 31 field inspectors) from a headquarters in Port Moresby and 4 field support offices. There are currently 42 active export sites in PNG and so inspections are conducted on a fly-in fly-out basis.

### **Outline of verification process**

The PNGFA Field Services Division is responsible for the field monitoring of all forest operations in PNG. All operations are required to have 5 year, annual and individual setup logging plans and actual operations are to be conducted in accordance with the "Papua New Guinea Logging Code of Practice" that is approved by both the PNGFA and Department of Environment/Conservation and endorsed by the Prime Minister. The PNGFA has formal documented (publicly available) procedures for the monitoring, reporting and approval processes. The PNGFA has the power to close down operations that are not compliant with these approved procedures.

Before issuing the Export Permit for each shipment, the PNGFA Marketing Section checks that the company is operating within its current and approved quota, that royalty payments to landowners are up to date and that the export prices for each species are satisfactory.

The SGS involvement in the verification process begins at the time of initial log measurement (at the forest landing) where all companies are required to affix an official bar-coded tag provided by SGS. This log number (which includes a unique site-code identifier) is used right through the verification process to export. SGS will only issue these tags when advised in writing by the PNGFA that the company has authority to harvest the area under one of the permit arrangements outlined earlier.

Then, at least two weeks prior to the impending log shipment an exporter must notify SGS so that inspection arrangements can be put in place. At the export port exporters must provide the SGS inspector with a log list in both electronic and hard copy format. The SGS inspector undertakes a pre-shipment inspection which involves a scaling check (10%); species check (100%) and verification that the volumes and species mix are as per the PNGFA Export Permit. Exporters are notified of any discrepancies and only if the results are satisfactory will the PNGFA officer on site permit ship loading to commence.

The SGS inspector then monitors the actual ship loading by removing a section of the bar-coded log tag and produces an independent tally of loaded logs. SGS has provided the inspectors with bar-code readers and portable computers to facilitate efficient and accurate preparation of all reports during the inspection process. An SGS Inspection Report is issued at the completion of loading. This Inspection Report is used by all Government Authorities to check the commercial and shipping documentation and clear the shipment for export.

All field inspection documents and reports are sent into the SGS head office which also receives copies of all shipping and commercial documents directly from the exporter. All this information is entered into a central database. A number of checks are made, for example, to

confirm that the export volume and prices for each species in a shipment are as approved by the PNGFA (through the Export Permit issued prior to shipment); that a project is operating within its approved log export quota and that the export tax paid has been calculated correctly.

Any serious discrepancies are immediately brought to the attention of the relevant Government Authority – usually the PNGFA or Customs Office. Monthly reports are also provided to a wide range of Government Authorities to assist them with their audit and monitoring functions. In addition to the PNGFA these include the Central Bank (foreign exchange remittances), Customs (export tax) and the Tax Office (export earnings declared on company tax returns).

The central database maintained by SGS has also been useful to verify if shipments declared as being from PNG have in fact originated from this country. There have been examples where logs have been detected in other Asian countries with documents purporting to show they are of PNG origin. In some cases a check of the SGS database was able to confirm that these documents were false and that the logs are therefore illegal. In other cases the same check revealed that the logs were indeed exported from PNG via the legitimate process.

## **SCHEME TO CHECK FOR LEGALITY AT THE TIME OF LOGGING**

### **Definition of legality**

While there is no formal and separate “Definition of Legality” in the context of the PNG forest industry, operators must follow the requirements of the Forest Act (1991) and there are a number of checks and balances in the PNG log export system that confirm many aspects of legality. Specifically.

Official log tags are not issued to any company unless the PNGFA confirms that they are a legitimate operator. This means that all logs inspected by SGS come from areas that have officially approved for harvest by the PNGFA through the Timber Permit or contract processes described earlier in this paper. All forest operations are required to comply with PNGFA regulations covering planning, operations and monitoring. Operations are also required to have their Environmental Plan approved by the Department of Environment and Conservation and follow Department of Labour regulations governing workers health and safety plus the employment of foreign workers.

Each export shipment must have a formal price approval and subsequent issue of an Export Permit by the PNGFA. As mentioned earlier the PNGFA completes a verification process prior to issuing this Export Permit which includes checking the log price and volume plus confirming that royalty payments due to traditional landowners are paid up to date. An Export License is required separately for each shipment from the Department of Trade and Industry.

SGS will not even commence an inspection unless there is evidence of all these requirements having been fulfilled. The SGS inspection confirms directly that the log measurements and species identification are accurate and that the volume and invoiced amounts on commercial trade documents are as legally approved by the PNGFA.

Subsequent checks in the SGS head office confirm that the export tax legally due has been paid in the correct amount and that logs have been cleared through the export procedures of all relevant PNG Government Authorities.

In more than 12 years of operations to date, SGS has not detected any instances of log smuggling. This therefore means that all of PNG’s log exports for this period (25 m m3) have been independently verified as having met the legal export requirements outlined above. By providing some information of shipment details, the extensive database maintained by SGS can also be queried for verification by overseas log buyers to confirm that they are dealing with a legitimate PNG export.

## **Procedures for retaining and verifying the evidence**

The role of the PNGFA Field Services Division staff in monitoring the day to day operations of the logging companies has already been outlined. They follow clear documented procedures for monitoring short and long term logging plans plus they undertake field checks to verify that the PNG Logging Code of Practice is being followed.

SGS are provided with copies of official Government documents: Export Permit and Licence (which detail approved volumes and prices). Log lists are provided to SGS inspectors who then verify the data in the export log yard by check scaling 10% of the logs and confirming the species identification of the whole shipment. Any discrepancies are reported to the exporter and local PNGFA supervisor in writing. Logs actually loaded onto a vessel are tallied by SGS who then issue an Inspection Report. Again copies are provided to the exporter and PNGFA.

In the SGS head office, the results of the inspection activities are checked against the commercial documentation and Government clearance documents (e.g. Export Entry) for any discrepancies. All information is entered into a central database from which are generated regular monthly reports plus special purpose reports on demand for stakeholders (generally Government agencies). All documents are stored in a permanent archive in case they are needed in future as evidence by the PNG Authorities.

## **CHAIN OF CUSTODY**

### **PNG requirements**

There is no formal chain of custody system implemented across the PNG forest industry. However, the number on the SGS log tag (used for export verification) is also the official log number used by companies to declare their monthly production records to the PNGFA. For each number (log tag) this declaration includes location (concession only), species, diameter, length, volume and landowner.

So it is possible to trace a log back to a concession and landowner area. However, the production records are held in hard copy in Provincial PNGFA offices and so tracking is not easy. Company records can be used but this presents an obvious

problem with lack of independence. There is potential in future for all the log production and log export records to be stored in a single database. This would constitute the beginnings of a national log tracking system and this is under consideration by the PNGFA.

### **Chain of custody verification**

As there is no formal CoC system there cannot be a formal verification system. However, as already explained SGS does check the measurement and species identification of export logs and as the number used is the same as that used by the company to declare its production records to the PNGFA. Therefore it is possible to check if there have been any unauthorized changes to individual log records.

## **FUTURE TASK AND PERSPECTIVES**

### **Criticisms and problems with the system**

At the time that SGS was contracted to be the independent monitor of log exports, the major concern of many stakeholders was the perceived revenue losses that had been occurring through various transfer pricing mechanisms. The export monitoring system run by SGS has largely countered this. However, as is occurring in most countries with tropical rainforest resources, issues are being raised by international stakeholders (particularly through the efforts of ENGOs) over legality of wood sources and wood production from a much wider perspective.

In PNG, recognizing that log exports are largely under control, this is focusing on social and environmental concerns and perceived breaches of PNG Government laws and regulations covering these issues. On paper, the regulations and monitoring systems of the PNGFA are very strong but in practice, as is often the case in developing countries, resources such as sufficient staff and logistical backup are lacking due to funding constraints. Also, Government Departments other than the PNGFA are responsible for monitoring key aspects such as social and environmental issues. These Government Departments also have funding and performance issues that prevent them from performing all their mandated tasks. Thus it is very difficult for the PNG Government to be certain that all its laws and regulations are being followed.

The key issue of customary landowner permission has been highlighted earlier. ENGOs argue that for many or even all forest concessions, the awareness process and gaining of permission have been inadequate. While this may be true of some areas, in practice it is very difficult to have a long lasting consensus that involves 100% of customary landowners in a forest concession. Groups or factions in an area (who may have been traditional enemies for generations) can struggle for a dominant position in the decision making process and new generations may disagree with decisions made by their older relatives. No matter how careful the consultation process has been it is nearly always possible for groups like ENGOs to find disgruntled landowners who may or may not be justified in their concerns. This can almost be described as a problem of democracy where the majority rules.

Some stakeholders would like to see independent monitoring extended back into the forest and to include legal compliance issues such as harvesting practices, environmental controls, plus the rights of traditional landowners and workers. The lack of a formal link between log production and log export records is also a problem that was described earlier. This prevents easy reconciliation of records.

The SGS monitoring system only covers log exports and not processed wood products. Although PNG's forest exports are dominated by logs the processing sector is gaining in importance at an increasing pace. Currently there is a lack of accurate statistics to monitor and support this desirable trend.

As with any system involved with legal verification, there are criticisms that there is no verification of sustainability – the major objective of most concerned stakeholders. However, the present PNG log export monitoring system does provide an important building block on which to build legal and sustainability verification systems.

### **Potential solutions and improvements**

PNGFA is considering the development of a legal definition for PNG forest operations to assist companies and the Government to demonstrate legal wood production. The development of such a definition would need an extensive stakeholder consultation process to ensure maximum credibility.

The PNG Forest Industries Association (whose members are responsible for 80% of PNG's forestry production) is also very interested in seeing the development of a legal forestry standard for PNG which can be adopted on a voluntary basis by their members. This would offer their international buyers assurances regarding the legal origins of their log sources and legal compliance of their production processes. SGS is already consulting with the PNGFA regarding the process and issues involved. This voluntary verification approach would be funded by the operating companies and would thus overcome the funding and co-ordination issues that make it difficult for a range of Government Departments to offer the assurances increasingly required by international trade.

To facilitate improved chain of custody verification that must go hand in hand with such legality verification, the PNGFA is considering the development of a single centralised database to hold all log production, processing and log export records. This could be implemented as a logical extension of the existing SGS export database.