

LEGALITY MANAGEMENT SYSTEMS OF TIMBER LOGGING AND TIMBER PRODUCTS SUPPLY FOR EXPORT VALID IN THE RUSSIAN FAR EAST.

Alexander N. Sidorenko
Dalexportles Association of Timber Exporters, Far East, Russia

GENERAL OVERVIEW

Dear ladies and gentlemen! Dear participants of the seminar!

I am thankful to the organizers for a kind invitation and opportunity to introduce a management system for legality of raw materials origin in the Russian Far East.

Several monitoring systems for legality of timber harvesting and timber products supply for export exist on the territory of the RFE:

- The state system is based on more than 30 legislative acts, and over 15 forestry ministries, agencies and departments are involved in this process.

Since the above laws are our internal laws, it is obvious, that there are very few people from other countries who are familiar with the real situation in the Russian Timber Industry Sector, and with the Russian system of forest use and management in particular.

- Dalexportles Association (DEL) Verification System and
 - SGS VLTP System.
- I'll briefly describe each of them.

THE STATE SYSTEM FOR LEGALITY CONTROL

The state system covers all stages of the forest business. In the thirties of the last century the research of the forest stock of Russia was started. The strict centralized regime, the state ownership on everything without exception and a planned economy required regular inventory of the whole property of the Soviet Union of that period. A unique system of total inventory and control has been established in each area and for each branch in the Soviet Union, including forestry. All forests have been divided into districts and allocated to the state timber industry incorporations.

The forest inventory enterprisers organized for that purpose have thoroughly studied and described the species of the forest stock, its density and age on every allotment. The forest stock study and inventory is carried out regularly to present day. They have also preserved the system of distributed and allocated plots of forest stock to timber industry enterprises.

The state grants plots of the forest fund to the forest users for a long-term lease up to 49 years. At the same time they estimate the legal status of a company- lessor, its business solvency and social responsibility.

The forest plots are granted in compliance with the

long-term state policy in sustainable forest management. There is a considerable number of territories, where forest use is either restricted or completely prohibited. Such restrictions are mainly related to environment protection issues, water protected area areas, etc. At this stage the federal laws, the Forest Code and Tax Code regulate the company's activities.

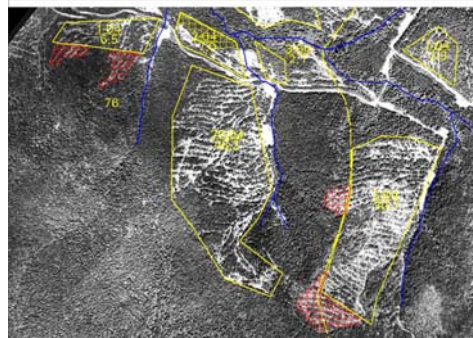
The enterprise develops a cutting plan and other activities for harvesting in accordance with the state regulations. The annual volume for harvesting is limited by allowable (prescribed) cutting, providing a sustainable forest management in the allotment of the leased forest fund. The observance control for cutting volumes and technology, ecological issues compliance is provided by the state inspections: Rosleskhoz, Rosprirodnadzor, Rosselkhoz nadzor, Ministry of Natural Resources, Ministry of Forestry Industry, environmental departments at the Government of each territory, the subject of the Russian Federation.

Responsibility for violation of legislative acts and regulations under the above mentioned state departments is various and depends on the degree of the violation. Punishment varies from a financial fine to the enterprise's right deprivation on lease of a forest plot; whereas a criminal liability can be applied to the head of the company. The infringer practically risks losing his business and freedom.

Under the results of the logging operations, the forestry industry enterprise submits a declaration that informs the state of the work performed: harvest volumes, place of logging, etc.

After submission of the declaration on logging executed, verification procedure of the data officially announced and the actual data starts.

Both land survey and aerial photography from planes and satellites are used to perform verification.



Drawing 1. shows the processed aerial photography images.

Using the analysis of the aerial photography results, one could see the violations, including the compact undercut and harvesting outside of legal boundaries. Moreover, the aerial photography allows disclosing the signs of large environmental disruptions.

The violations detected from aerial photography are double-checked and verified by land survey. The land survey is also used to identify smaller ecological disruptions. 1580 people, the forest unit workers, carry out the land inspection in the Khabarovsk Territory. The results of all kinds of control are compared, analyzed and issued for further decision-making.

The further control over the legality of wood product supply for export under the state system is assigned to Rosselkhoznadzor and the companies-carriers. At dispatch station, while being transported in the other region, Rosselkhoznadzor checks timber at the storage place and prepared for shipment for legality. The quarantine certificate, which indicates the volume and structural parameters of the timber products for shipping, is issued.

Weighing of loaded cars at large transit terminals also allows disclosing violations, related to illegal overweight of cars, when the real volume of the timber products exceeds the volume declared in a waybill. The most frequent violations are the ones executed by doubtful companies, when they deliver timber to People's Republic of China via Grodekovo Terminal. If infringement occurs, the fine is five times the amount of the transportation fee.

Upon the freights' delivery in ports, the goods are put into customs control zones. Rosselkhoznadzor watches carefully that all cars, arriving to a port and loaded with timber products, have quarantine certificates. Rosselkhoznadzor inspectors together with the VNIIEK specialists (All-Russia Scientific Research Institute for Plants Quarantine) inspect timber again, calculate quarantine certificates issued at the place of shipment, verify with the actual number of certificates at the storage area and issue a unified phyto-quarantine certificate for all ship consignment.

The customs inspection precedes timber products' loading on board a ship. In this case the procedures are regulated by the Customs Code. The Customs bodies build their work upon the conclusions made by Rosselkhoznadzor, Chamber of Commerce and Industry expertise and other independent expert reports, concerning the quantity and quality of the goods to be shipped for export. The Customs also performs its own inspection of the goods ready for shipment for export. After completing loading the Customs issues a Cargo Customs Declaration, which confirms the legality of timber products shipped for export.

It's obvious that a Cargo Customs Declaration cannot provide a hundred percent guarantee for the product legality. We acknowledge that we have such violations but the state is fighting against those and the violation's number is getting reduced.

The violations are divided into two major categories:

1. Illegality of harvesting, causing damage to the environment;
2. Illegality related to economic violations in forestry business.

Illegal harvesting in Russia is rather limited due to the existing system of overlapping satellite and airplane control. The above violations and the persons at fault could be easily identified and punished. In this connection, the number of violations in the harvesting process is gradually dropping.

It's more complicated to control the economic violations in the forestry business, where the major violation is deviation from taxes payment. Unfortunately, the similar violations are typical for all other branches of industry and not only in this country.

One of most significant issues is the price making procedure for the timber products to be sold is a rather serious process. The price is defined and established between a seller and buyer individually, upon their discretion and depends on many factors. On a monthly basis, the State Customs Committee sets up the prices minimum level, recommended for usage by the customs throughout the territory of Russia, when determining the customs value of the goods for export, including the timber products.

In case the exporter declares the price lower than the fair value, the customs shall correct the export duty, using the legislative act- Adjustment of the Customs Value. However, because of the unfair actions during price making (double invoices), a gross violation of the Russian Currency and Tax legislation occurs. It happens when a seller asks a buyer to transfer only a part of the sum to an account in Russia, whereas the rest would be transferred to various bank accounts. In this case the customs duties do not suffer, but the state budget receives less of the tax revenues, and an unfair exporter receives an additional illegal profit, saving on taxes.

It's a serious infringement of the Federal Law No.173- Φ 3 of December 10, 2003 "On Currency regulation and currency control", Chapter 3, Article 19 and is penalized by fine from three fourth up to one size of the sum of money resources, which have not been paid onto the accounts in authorized banks ". Point 4, Article15.25. of "the Code on Administrative violations " of December 30, 2001. No.195- Φ 3.

The Currency Control Bodies of the Central bank of Russia observe this kind of infringement through the agent banks, realizing settlement operations under foreign trade contracts. Under such infringement the underestimated base for the taxation is formed. Only after receiving all amount of money for the sold goods on his account, the seller has the right to transfer money to any account of any country if necessary.

This significant infringement is very difficult for monitoring from Russia. The Customs follows the unified (indicative) prices. If the prices of the sale are lower than the indicative prices, the Customs have no right to either forbid export of the goods or make any obstacles, but will only increase the duties up to the level of the

recommended (indicative) prices. The attempts of the Customs to stop export of forest products under the illegal prices have been challenged in courts by the sellers. The function of the customs is to collect duties for the goods crossing the border, and the customs is not a commercial organization to define what price is fair and what price is not fair.

However, the Japanese companies –buyers can render a great help to the Russian party in stopping the above violation, which we call “ the illegal price”, and consequently in stopping the illegal timber products supply. From now on the Japanese buyers know that all money should be transferred to an account of the seller, specified in the contract and if a Russian seller asks to transfer money to several accounts, using double invoices, it means an illegal activity.

The purpose of any illegal activity, in most cases, is to receive additional revenue, which is impossible when you observe the legislation.

The illegal activity is accompanied by reduced costs at timber harvesting, when every sort and kind of regulations and legislative acts are violated, the environmental sustainability is infringed.

The State Control System struggles against the above mentioned violations.

Illegal activity is also accompanied by a product value hidden from taxation- it's the trade using double invoices under “illegal price. At this stage we are applying our Japanese colleagues for support and interaction and not to purchase forest products from Russia for which it is necessary to transfer money onto accounts not specified in the contract. It is an illegal purchase.

VERIFICATION SYSTEM FOR LEGALITY BEING IMPLEMENTED BY TIMBER EXPORTERS OF DALEXPORTLES ASSOCIATION

Besides the State System of Control, there exists the verification system on legality for timber harvesting and timber supply for export, being implemented by Dalexportles Association.

This work started after the moment the Memorandum between Dalexportles, the Far Eastern Timber Exporters Association and Japan Lumber Importers Association was signed in Khabarovsk, Russia in April 2006.

In accordance with the Memorandum the Russian exporters have to confirm the origin of raw timber for legality using one of the existing systems, that is by receiving the certificates of sustainable forest management.

Taking into consideration that receiving of the certificate under “FCS” system takes long time, it has been agreed to accept the guarantee from Dalexportles Association as the provisional measure for the above period.

The collective verification system on legality for timber harvesting and timber products supply for export, being implemented by Dalexportles Association, is as follows:

- 1) Above all, a company should be the member of DEL;
- 2) The Association appoints a commission of experts, consisting of the representatives of the auditing company, Far East Forestry Research Institute and representatives of the Executive Board of Directors of DEL Association.

The items under verification are subject to the policy of the Association, developed for the purpose of the verification on legality for timber harvesting and timber products supply for export.

The appointed commission of experts receives from the enterprise - applicant answers to the questionnaire, totaling 78 points.

The questions are categorized under the following headings:

1. The legal status of a company
Law observance/compliance of a company-applicant is verified at the stage when the company issues shares and undergoes the procedure of registration as the business representative.
2. Access to land and forest fund
Under this item the legality for harvesting operations right acquisition is verified; contracts, providing the foundation for the allotments of forest fund granted to a company –applicant, are examined, fulfillment of obligations by the company-applicant under the signed contracts is assessed.
3. Timber products manufacture technology
The expert team studies the harvesting technology and its compliance with the law and regulations
4. Quality management system
Regulations observance of storing, measuring, grading and inventorying of timber products
5. Sustainable forest management
It includes observance of legislation requirements in terms of environment protection, reforestation, forest fire protection, utilization of all timber products assortment, etc.
6. Enterprise management systems

Completeness and correctness of tax and other obligatory payments is examined. The established level of salaries and obligatory payments to budget and non-budget funds is studied.

I would like to point to the fact that the companies, optimizing the above item, that is applying illegal schemes for reducing tax fees, do violate the Law. Besides, they have an opportunity for receiving excess profits, and consequently expanding their illegal activity.

It should be noted that the examination for completeness and correctness of the tax computation is a distinctive feature of the verification system being implemented by Dalexportles Association, compared to other acting systems.

7. Timber products traffic monitoring
Warehousing methods, inventory of timber product traffic in the warehouse and observance of the Customs Code is attested at this stage.

The attention is focused on the value of the product to be sold at this stage.

The Association informs the company-applicant of the expert commission assessment results and its decision, which either confirms the legality of harvesting and wood products supply for export, or rejects it.

- 3) In case the company-applicant is not the Dalexportles Association member, the former can apply for a membership.

The observance of laws, reputation –are the values, highly respected by the Dalexportles Association members. We are happy to state that more and more companies share our views and approaches are ready to become DEL Association members and be verified for legality of harvesting and wood products supply for export.

SGS VLTP VERIFICATION SYSTEM

Besides the above described State Control System for legality of the raw timber origin and its supply for export AND the collective verification system being implemented by Dalexportles Association, the Validation of Legal Timber Programme (VLTP) is being realized on the territory of the Russian Far East. The Programme is represented in a separate block and I shall only briefly report on it.

Validation of Legal Timber Programme (VLTP) is the part of a global Forestry Monitoring Programme, which operates in 145 countries. The objective of the Programme is to contribute to international, national and regional initiatives aimed at struggling the illegal timber harvesting and trade of illegally produced timber products. The concept of the Program meets the requirements of international initiatives for fighting the illegal forest management.

In the Russian Far East SGS VLT Programme is being implemented under the Territorial Governments within the state- private partnership framework on a voluntary basis. "Legality verification" under SGS VLTP is considered as an alternative, but additional and useful stage in the sustainable forest management verification process.

Program management is realized by SGS in partnership with the local organization, the Center of Forest Certification, through the VLTP Agency, set up in Khabarovsk, Far East of Russia.

Verification methods for legality include: data collection and cross analysis of the information received from the companies and competent state bodies, undeclared inspections of production areas, continuous monitoring of industrial operations, data analysis of the timber products manufacture in dynamics and data analysis of the remote monitoring.

CONCLUSION

It's quite obvious that of the above-introduced systems for verification on legality for timber harvesting and timber products supply for export, the State Control System is the most powerful and effective one. It consists of a great number of overlapping verification sub-systems, which double-check each other in some cases. The State Control System is responsible for reliability of the information provided or for hiding of information. At the same time the companies under inspection bear responsibility for violating the Law. The system of ecological safety has always been an old tradition in Russia.

I can gladly note that we at present we observe the interaction of the representatives of different controlling institutions and determination of the timber industry companies to conduct a responsible and legal business and it's the most important tendency. We all realize that legal, transparent and sustainable business is the guarantee for our future