

**Statement of Alexander von Bismarck, Campaigns Director
Environmental Investigation Agency
to the
Trade Policy Staff Committee
on the
Priorities of the United States-Malaysia Free Trade Agreement**

May 15, 2006

Introduction

Chairman and Members of the Trade Policy Staff Committee:

The Environmental Investigation Agency (EIA) values and appreciates this opportunity to present our expertise on issues relating to the preliminary negotiations of a Free Trade Agreement between Malaysia and the United States.

2. EIA has investigated international trade in environmentally sensitive products for twenty-one years and is globally recognized for its analysis of the trade in illegal timber, wildlife and ozone-depleting substances.

3. EIA has also focused on the particular impacts of Free Trade Agreements (FTAs) on these issues. We have closely tracked the US-Singapore Free Trade Agreement (USSFTA) and released a report in May 2003: *Singapore's Illegal Timber Trade & the US-Singapore Free Trade Agreement*.¹ EIA submitted testimony to the House Ways and Means Committee on the environmental impacts of the USSFTA and also recently testified to the US House Committee on International Relations, Subcommittee on Africa, Global Human Rights and International Operations on China's role in the African timber industry.

4. Since 2001, EIA investigations, combining data analysis and on-site undercover visits, have revealed Malaysia's role in the regional illegal timber trade. Much of this information can be found in the report, *Profiting from Plunder: How Malaysia Smuggles Endangered Wood*.² More recently, EIA has held a series of constructive high-level meetings with government officials and industry representatives in Malaysia to discuss actions that may be taken regarding the regional illegal timber trade, including the Ministry of Plantation Industries & Commodities; Ministry of Natural Resources & Environment; Malaysian Timber Council; Malaysian Timber Industry Board; Sabah Forest Department; Sarawak Forest Corporation; Sarawak Timber Association; Timbers Exporters Association Malaysia; Malaysian Wood Moulding and Joinery Council; the US, Indonesian and UK Embassies in Malaysia; and several Malaysian-based NGOs, among others.

¹ Available at: <http://www.eia-international.org/cgi/reports/reports.cgi?t=template&a=54>

² Available at: <http://www.eia-international.org/cgi/reports/reports.cgi?t=template&a=67>

The Global Illegal Logging Problem and its Affects on US Industry

5. Illegal logging takes place when timber is harvested, transported, bought or sold in violation of national laws and is pervasive in many of the major timber producing and exporting countries of the world. In many countries, illegal logging represents the majority of production; therefore large quantities of illegally-sourced wood products find their way to the major markets of the US, Europe, Japan and China.

6. Illegal logging has devastating economic consequences around the world. It is estimated that illegal logging on public lands alone causes annual revenue and asset losses to governments of \$10-15 billion.³ Indonesia in particular, who shares a long border with Malaysia, reports losses of \$3.7 billion annually.⁴ This lost revenue could be funding schools, hospitals and providing clean drinking water in developing countries but is instead diverted to the bank accounts of illegal timber barons, corrupt enforcement personnel and politicians.

7. Illegal logging hurts U.S. industry. Wood products made from illegal timber benefit from the cheap raw material input and avoid the costs associated with legal production, such as paying for management plans, stumpage fees, duties and tariffs. These products can then be sold in the US at a discount price, thus undercutting the US timber industry. The American Forest & Paper Association estimates that US timber producers lose approximately \$1 billion every year due to global illegal logging: \$460 million from the lost ability to export to foreign markets and \$500-700 million due to depressed prices caused by illegal material in the market.⁵

Malaysia's Role in Bringing Illegally Logged Timber to the United States

8. Malaysia is one of the main sources of illegally logged timber reaching the United States market. According to the US International Trade Commission, the US imported \$223 million worth of Malaysian tropical hardwood products⁶ in 2005, comprising 11% of global US tropical hardwood imports.⁷ Since Malaysia's timber industry is highly export-oriented and cannot rely on its own forests for supply, a significant percentage of Malaysian wood products exports are derived from imported raw material, much of which has been shown to be illegal. For example, Indonesia's own Forestry Ministry estimates that 80% of its country's harvest is illegal,⁸ yet Indonesian forests support much

³ The World Bank, "Sustaining Forests: a development strategy," 2004.

⁴ Indonesia Ministry of Forestry data, as reported by *Dow Jones Newswires*: "Tarkett AG Denies Illegally-Sourced Merbau From Papua," 4/19/06.

⁵ Seneca Creek Associates and Wood Resources International, "Illegal Logging and Global Wood Markets," 2004, available at:

http://www.afandpa.org/Content/NavigationMenu/News_Room/Papers_Reports1/Whitepapers.htm

⁶ "tropical hardwood products" is defined as the following 6-digit codes within the US's Harmonized Tariff Schedule: 4403 (31), (32), (33), (34), (35), (41), (49); 4407 (21), (22), (23), (24), (25), (26), (29); 4408 (31), (39); 440920; 4412 (11), (13), (27), (29), (99).

⁷ reports run on the US ITC Trade DataWeb System

⁸ Available at: www.illegal-logging.info/news.php?newid=241

of the Malaysian timber industry. Even more explicit, 77% of Malaysia's reported sawn wood imports are from Indonesia,⁹ which currently has a sawn timber export ban.

9. Due to their current dependence on illegally logged raw materials, imported Malaysian timber products threaten to undermine the U.S. Government's initiatives to control illegal logging. These include President Bush's Initiative Against Illegal Logging, the G-8 nation's March 2005 commitment to tackling illegal logging and the recently announced US-Indonesia bilateral on illegal logging. EIA investigations and other studies, highlighted below, have verified that undocumented wood from Indonesia likely provides the base of the Malaysian wood processing industry.

Laundering Illegal Indonesian Timber

10. Unlike many other producer countries in the region, middle-income Malaysia has had the resources and governance structures necessary to keep illegality in forest production to a minimum in recent years. Unfortunately, while drastically reducing its domestically sourced raw materials, Malaysia has maintained a massive industrial timber processing and export capacity. A 2001 World Bank study found Malaysia's installed capacity to be 40 million cubic meters, while domestic log production was only 22 million. By sourcing increasingly from abroad, Malaysia has been able to maintain its position as the largest exporter of tropical timber in the world.

11. Unfortunately, much of the material imported into Malaysia, especially from Indonesia, is illegal. An independent study found that Malaysia's use and export of timber in 2001 exceeded available supplies from legal cutting and import by more than 13 million cubic meters. The study concluded that the difference most likely represented illegal wood, principally sourced from neighboring Indonesia. Consequently, though illegal logging within Malaysia is limited, the percentage of Malaysian timber and wood product exports of dubious origin is likely to be very high.

12. During the last five years, repeated and detailed evidence has been provided by EIA and others of large scale import and re-export of illegal Indonesian timber, while successive Indonesian governments have requested action by the Malaysian government to halt the cross-border trade. Most recently, the Malaysian government has refused to block import of rough sawn-timber arriving from Indonesia despite the Indonesian government's 2004 ban on export and a request for reciprocal enforcement.

Ramin & CITES

13. Ramin is a valuable blond tropical hardwood endemic to Indonesia and Malaysia. The species was the first major commercial timber targeted by the industry in the two countries, and as a result is now very rare outside of protected areas. In 2001, following evidence of widespread illegal logging of ramin in national parks, Indonesia listed the species on Appendix III of the Convention on International Trade in Endangered Species (CITES), making it a requirement for CITES documentation to accompany all shipments

⁹ ITTO, "Annual Review and Assessment of the World Timber Situation," Appendix 2, 2004

of ramin timber and wood products traded internationally. Indonesia simultaneously banned almost all cutting and export of the species, and other than for a small amount of wood originating with a single company, no ramin has been granted a CITES export permit by the Indonesian government since December 31, 2001.

14. The only other country where ramin wood grows is Malaysia, and as a CITES signatory the listing should have required Malaysia to halt all imports of ramin from Indonesia and issue CITES permits for exports. However, the government first refused to implement the listing fully by taking out a reservation against the inclusion of processed wood products. Later, EIA investigations revealed that the Malaysian government had also failed to implement the listing for logs and sawntimber. A series of exposes on cases of illegal Indonesian ramin entering Malaysia without CITES permits culminated in late 2003 in an investigation which revealed widespread laundering of illegal Indonesian ramin on an unprecedented scale, involving quantities of stolen timber greater than the global legal ramin supply. This information was released by EIA in early 2004 in the report *Profiting from Plunder: How Malaysia Smuggles Endangered Wood*.

15. The illegal ramin trade facilitated by Malaysia prompted seven NGOs in 2004 to file a *Pelly Petition* to the US Government requesting that the US impose trade sanctions on Malaysia. This action can be used when “nationals of a foreign country, directly or indirectly, are engaging in trade or taking which diminishes the effectiveness of any international program for endangered or threatened species.”¹⁰ The petition is still pending.

16. After initially denying the existence of a problem, the Malaysian government eventually acted on the evidence in the report and the Pelly Petition, where they made the largest seizure of illegal ramin ever recorded. Though Malaysian officials confirmed that the ramin had originated in Indonesia and was not accompanied by CITES permits, the timber was released for onward shipment because Malaysian law does not implement CITES in free trade zones. Though legal basis to seize the wood on arrival existed in the destination ports in China, Hong Kong and Taiwan, warning letters from Malaysia to the destination ports were sent too late for action to be taken.

17. In 2004, responding to concerns over continued illegal trade in the species, global governments voted to increase the controls over ramin trade and listed the species on Appendix II of CITES. Meanwhile, the loopholes and problems with Malaysian CITES legislation highlighted more than two years ago have yet to be remedied.

The Failure to Respect Indonesia's Bans on Export of Logs and Sawn-timber

18. Distinguishing legal from illegal timber presents considerable difficulties to enforcement officials in exporting and importing countries. In an attempt to assist enforcement against rampant illegal logging and timber smuggling, in October 2001 the Indonesian government banned all export of round and square logs.

¹⁰ 22 U.S.C. §1978a

19. Despite a commitment from a Malaysian minister to respect the Indonesian ban, subsequent EIA investigations in 2002 revealed fleets of small vessels loaded with Indonesian logs and flying Indonesian flags continuing to arrive unhindered at numerous ports along the west coast of Peninsular Malaysia, including Batu Pahat, Melaka, Kuala Linggi and Muar, in full view of customs officials. While initial private alerts sent to the Malaysian government failed to elicit a response, widespread international media attention eventually led Malaysia to pass a reciprocal import ban for Indonesian logs. The ban was not properly implemented until a year later, however, following further media publicity.

20. Though the Indonesian log ban and the reciprocal Malaysian control did result in a dramatic reduction in illegal cutting and trade in source areas, the smugglers soon adapted and began roughly sawing the timber in the forest before shipping. EIA investigations in 2003 and 2004 revealed that illegally-sourced rough sawn timber blocks and planks continued to flood into Malaysia through the west coast ports and through land and sea entry points in the East Malaysian states of Sarawak and Sabah.¹¹ In one example, an EIA aerial survey in 2004 documented a network of roads stretching across the East Kalimantan-Sabah border, used to smuggle timber out of Indonesia to Malaysia.¹² Tempo, a respected Indonesian news magazine, investigated the Sarawak-Kalimantan border later that year and concluded that everyday, 120 trucks, carrying an average of 9 cubic meters each, smuggle timber across the border, resulting in almost 400,000 cubic meters annually. The investigators found that the wood is then shipped from Sarawak to Malay-controlled islands for export.¹³

21. Faced with ongoing smuggling of timber roughly hewn in the forest, in November 2004 Indonesia further banned the export of undried, rough sawn wood. Indonesia requested that Malaysia respect this new control by halting imports of the banned products, but no response has resulted. In late 2005, EIA sent detailed information regarding the continuing import of illegal rough sawn timber into Peninsular Malaysia and Sarawak, garnered during a series of field investigations in the summer of that year. No response was received and Malaysia continues to officially permit the import of Indonesian rough-sawn wood for use by the country's export-oriented timber processing industry.

Malaysian Companies Driving Illegal logging around the World

22. A 2005 EIA report exposed what was believed to be the largest single trade route of stolen timber in the world. It outlined how \$600 million worth of merbau, a dark hardwood that grows primarily in the eastern Indonesian province of Papua, was being illegally logged and smuggled out of Indonesia to China every month. The racket involved shipping brokers in Singapore, traders in Hong Kong and buyers in China and India, but much of the financial backing came from Malaysian-based companies and Malaysian nationals in Indonesia. Before the report release, Papuan police had identified

¹¹ EIA, "Profiting from Plunder"

¹² EIA/Telapak internal report from field investigation, October 2003.

¹³ Tempo, "Investigation traces Indo-Malaysian illegal timber ring," August 9, 2004.

68 suspects involved with illegal logging, 42 of which were Malaysian. After releasing the expose, EIA provided Indonesian authorities with the names of 32 financiers, and Indonesian police confirmed “that most of the financiers of illegal logging in the country were Malaysians.”¹⁴

23. Indonesia promptly instigated a crackdown on illegal logging with a focus in Papua. On January 27, 2005, authorities arrested a Malaysian national whom they determined to be “financing the massive illegal logging operation.”¹⁵ Then in April, Indonesian police arrested another Malaysian, whom they “suspected of masterminding the smuggling of illegally logged timber from Papua to Malaysia, as well as running illegal logging operations in Borneo.”¹⁶ By the end of that month, ten Malaysians, along with 60 Indonesians had been arrested.

24. Included in this ring was a financier tied with Rimbunan Hijau Jaya, linked to Malaysian-owned logging conglomerate Rimbunan Hijau. Rimbunan Hijau has a well-documented history of human rights abuses and illegal logging activities throughout the region. The timber conglomerate has been identified with illegal logging operations in Indonesia and Papua New Guinea, destructively logging vast areas of ancient forest and using the protection of political elites. A report on Rimbunan Hijau by the Papua New Guinea Department of Labour and Employment found widespread corruption, bribery and human rights abuses, including Rimbunan Hijau employees being treated like slaves by the company’s privately paid police squad and forced to live in appalling conditions in company-controlled logging camps.

Malaysian Political Position Regionally and Bilaterally

25. In 2001 the countries of East and South East Asia came together in Bali, Indonesia and agreed to a groundbreaking declaration on Forest Law Enforcement and Governance (the Asia-FLEG Declaration) which recognized the problems of illegal logging and its associated trade in the region and committed the relevant governments to take specific actions. The agreement included almost all of the major timber producing and consuming countries in the region, including Indonesia, Cambodia, Vietnam, the Philippines, Laos, China and Japan, plus the US and Europe. The only significant regional countries which were not part of the agreement were Malaysia and Singapore. Malaysia has yet to endorse the agreement.

26. In 2005, Malaysia and Indonesia began negotiations on a bilateral agreement to help halt illegal timber being transported between the countries. Indonesia has already signed such agreements with the UK, China and Japan. The Malaysian government has presented the ongoing talks as evidence of its commitment to help combat illegal logging in Indonesia, but it has recently become apparent that Malaysia’s purpose in the discussions is to ensure access to ready supplies of Indonesian timber for the country’s

¹⁴ The Jakarta Post, “More financiers of illegal logging put under arrest,” March 9, 2005.

¹⁵ The Jakarta Post, “Police nab illegal loggers,” February 23, 2005.

¹⁶ ABC Asia Pacific TV / Radio Australia, “Malaysian Nabbed for Illegal Logging,” April 21, 2005

industry. Rather than agree to simple joint measures for halting the trade of timber already banned from export, the Malaysian government is seeking to persuade the Indonesian government to relax its bans on the export of logs and sawn-timber. Supposedly Malaysia will commit to only accept logs and sawn-timber that have been legally sourced, but the only idea of how they might achieve this mentioned thus far is to limit the number of legal entry points. The reality is that this would only work if the Indonesian industry was under control, but illegal logging and timber smuggling remain rampant, and the reasoning behind bans on export of logs and rough sawn-timber remains. Aware of this, Indonesia is unwilling to relax the bans and the talks are apparently deadlocked.

27. Malaysia was also taking forward a prior notification system between its eastern states of Sarawak and Sabah and China, but this initiative has apparently been dropped. It seems that the Malaysian government has carefully considered this prior notification scheme, a reciprocal sawn timber ban and strengthened enforcement under a bilateral on illegal logging with Indonesia, and has made a deliberate policy decision not to continue with any of them. They are instead pressing forward with a strategy of encouraging Indonesia to lift the bans on log and sawn timber export to essentially legalize timber coming into Malaysia from Indonesia that has been illegally exported. These actions are clearly moving away from increased enforcement and show an unwillingness to deal with their role in the illegal logging problem.

Expected impact of the FTA: Lessons from the US-Singapore FTA

28. EIA fears that a US-Malaysia FTA will trigger a significant increase in Malaysian-controlled exports of illegally produced wood products to the US. While a FTA could offer excellent opportunities to cooperate and address problems of trade in illegally sourced timber, such opportunities have remained unexploited in past FTAs.

29. The US signed a FTA with Singapore in May 2003, which is also is a financial and physical hub in the global illegal timber trade. At the time, EIA published the report *Singapore's Illegal Timber Trade and the U.S.-Singapore Free Trade Agreement*, exposing criminal syndicates operating illegal timber trade rings from inside Singapore. Now, three years after the signing of the USSFTA, despite a President's Initiative Against Illegal Logging, the total achievements on environmental issues for this FTA consist of a Memorandum of Intent for environmental cooperation and an Action Plan, signed late last year, which has yet to result in any action that we are aware of. We are told that parties will meet regarding the Action Plan sometime this calendar year.

30. Since the signing of the USSFTA, Singapore's stature in the global illegal logging epidemic has increased. A major Washington Post investigative article published April 9th revealed that in 2005, 126,300 cubic meters of sawn timber was imported by Singapore from Indonesia, which was illegal under the Indonesian sawn-timber export ban. EIA analysis of customs data shows that during the first 10 months of 2005, US ports received at least 3,840 tons of Indonesian sawn timber via Singapore, up from 2,600 tons the year before.

31. Just as worrying is Singapore's role in financing and arranging far-flung global illegal trading schemes. The Post article reveals that last year the Indonesian money laundering authorities filed a report "about suspected timber smuggling involving more than 50 transactions from a Singapore bank account to two bank accounts in Indonesia," totaling \$10 million over two years. Additionally, EIA's 2005 report *The Last Frontier*¹⁷ uncovered the world's largest single illegal timber trade stream involving as much as 300,000 cubic meters of illegal exports from Papua to China each month and found Singaporean brokers arranging most of the transactions.

32. The record of inaction on environmental matters under the USSFTA is of grave concern for the impacts of a Malaysian FTA. A US-Malaysian FTA can be expected to have a more direct impact of increasing volumes of illegal timber reaching the US. As the *Final Environmental Review of the USSFTA* states: "international trade can play a role in stimulating, enabling, or rewarding illegal activities in a number of Asia-Pacific countries where illegal logging has been identified as a significant cause of deforestation." This statement is especially true for Malaysia, where a massive timber products manufacturing center allows illegal Indonesian timber to become Malaysian origin and thus directly covered under articles of a US-Malaysia FTA.

The Urgent Need For Demand-Side Measures

33. Therefore, it is imperative that major actions be taken as part of this FTA with Malaysia to ensure the health of Southeast Asian forests and communities and the US timber industry. A FTA with Malaysia presents great opportunity to encourage meaningful action to stop illegal timber imports from entering the US, but only if strong measures are incorporated into the agreement and promptly enacted. While the US has demonstrated a significant commitment to promoting international measures to counter illegal logging, including support for the several regional FLEG processes and the President's Initiative Against Illegal Logging, no policies or programs have emerged that will close or even restrict its massive domestic market to imports of illegally produced timber. The US remains the world's largest consumer of forest products, and its demand continues to drive illegal logging in poor developing countries to the detriment of the communities that depend in those forests, the governments that are losing revenue generated by those forests, and the US timber industry.

Recommendations:

- 1) The US should enter into a bilateral agreement with Malaysia as a condition to completion of a FTA. This bilateral would establish a licensing system to identify and separate legal from illegally-sourced wood products; thus allowing the elimination of trade in illegal goods. The bilateral should include dedicated staff on both sides to implement its goals.

¹⁷ <http://www.eia-international.org/cgi/reports/reports.cgi?t=template&a=93>

- 2) The United States must develop new legislative tools to stop the import, purchase, and/or sale of illegally produced timber, inline with its commitments at the last G-8 meeting that said: “We will act in our own countries. We will take steps to halt the import and marketing of illegally logged timber, for example by giving appropriate powers to our border control authorities through voluntary bilateral trade agreements or other arrangements.” The US should commission a study on the implementation of such legislation. Ongoing initiatives, such as those in the EU, offer templates.

- 3) During negotiations of the FTA, the U.S. should to encourage Malaysia to:
 - a) Support the establishment of a regional enforcement mechanism on illegal timber trade to identify and stop illegal timber shipments before they reach the US; Options for such systems have been developed in expert workshops this year.
 - b) Implement an import ban of Indonesian sawn timber that is reciprocal to Indonesia’ sawn timber export ban, which Indonesia has requested;
 - c) Require proper scrutiny of goods in transit, such as prohibiting the re-packaging and processing of goods in transshipment or under Customs control;
 - d) Commit to taking action to halt illegal logging and its associated trade in the region by formally endorsing the Asia FLEG Ministerial Declaration already agreed by most other regional governments in 2001, and by putting in place an action plan for the implementation of these FLEG commitments;
 - e) Effectively implement a Malaysian – Indonesian Memorandum of Understanding on illegal logging;
 - f) Support Indonesia’s proposal to allow NGO participation in the Ramin Tri-National Task Force set up by Singapore, Malaysia and Indonesia in 2004;
 - g) Issue a non-detriment finding for its trade in ramin wood (*Gonystylus spp.*), as required by Appendix II of CITES; and
 - h) Adopt a policy of transparency concerning its trade in environmentally sensitive goods and ensure transparent access to key data concerning trade with Indonesia, timber trade and wildlife products.

Thank you.