

NO CHIP MILL WITHOUT WOOD



A study of UFS projects to develop wood chip and paper pulp mills in Kalimantan, Indonesia

By: Betty Tio Minar

August 2006



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ABOUT DTE

Down to Earth - the International Campaign for Ecological Justice in Indonesia - is a UK-based campaigning organisation which works to support vulnerable communities to secure a just and sustainable future.

This work is rooted in a commitment to human rights, particularly the collective rights of communities to:

Land: land security for rural communities and the recognition of indigenous peoples' customary rights to land;

Participation: peoples' right to participate fully in the planning and governance of their communities and assets;

Environment: the right of communities to a clean and safe environment for their own survival and well-being.

Our work aims to ensure that decision-makers - particularly governments, international institutions and multinational companies - are held accountable for actions that impact on these rights.

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Cover photo: Haem-LPMA. Beach in Alle-Alle village



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in Kalimantan, Indonesia**

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MAP 1: Location of UFS Projects in Kalimantan

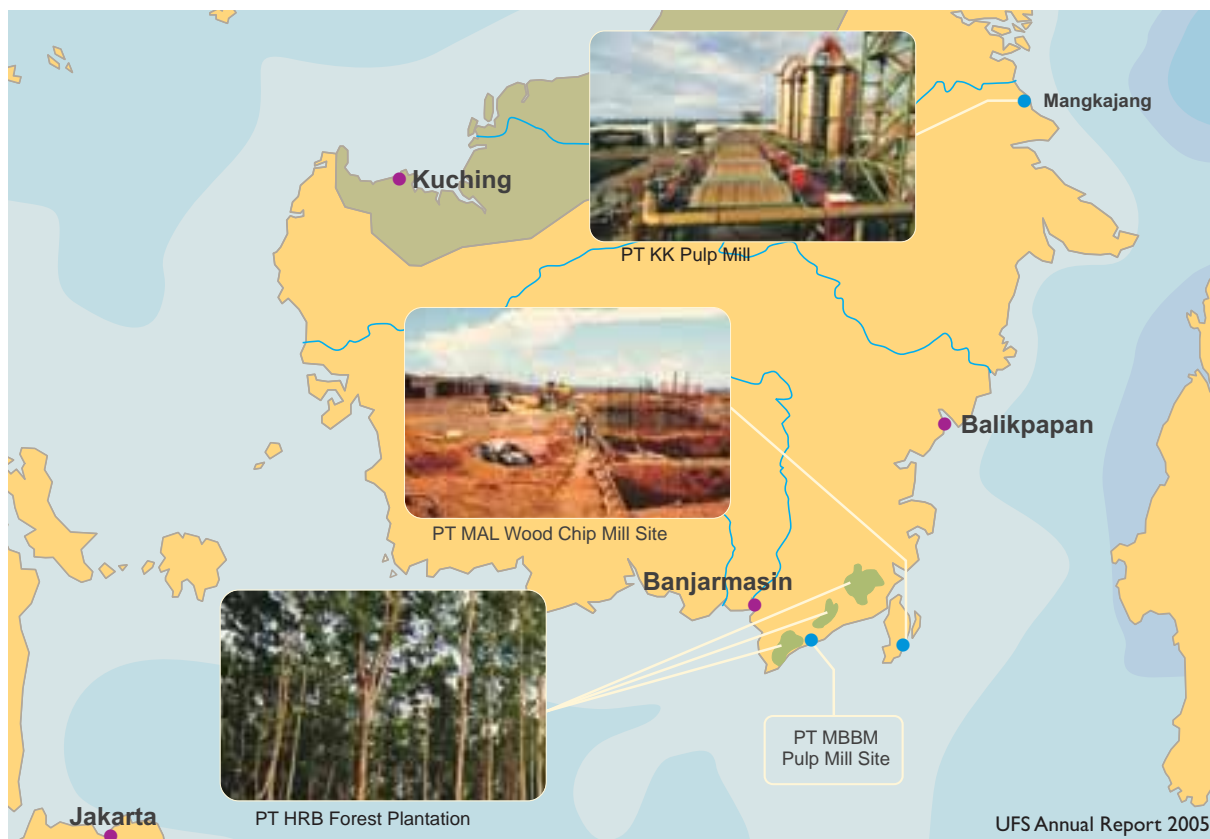


Table 1: UFS Project in Indonesia

Company	Activity	Location	Areal/ Capacity
PT MHB/HRB, Hutan Rindang Buana (previously known as Menara Hutan Buana)	Industrial Timber Estate Management (<i>HTI</i>)	Five plantation blocks in the southeast part of the South Kalimantan mainland	268,585 hectares
PT MBBM, Marga Buana Mulia	Development and operation of new pulp mill (US\$863 million) to start construction in 2007	Sungai Cuka, Satui, Tanah Bambu district, South Kalimantan province	600,000 tonnes pulp/year (possibly increasing to 1.2 Mt)
PT MAL, Mangium Anugerah Lestari	Development and operation of wood chip mill (US\$39 million) to start construction in early 2006	Alle-Alle village, southern part of Pulau Laut off the South Kalimantan coast	700,000 tonnes wood chips/year
PT KK, Kiani Kertas (negotiations for purchase in progress)	Pulp mill (set up in November 1999 by Bob Hasan). UFS took over production in July 2005	Malinau district, northern part of East Kalimantan province	525,000 tonnes hardwood kraft pulp/year

Source: Updated from DTE Newsletter 67:11

SUMMARY

The development of a wood chip and a paper pulp mill in South Kalimantan raises many questions and has stimulated debate in a number of circles. Indonesian and international civil society organisations and researchers have concluded that these projects, driven by the Singapore-based company United Fiber System (UFS), are completely unsustainable.

This report centres on a study of the wood chip plant under construction at Alle-Alle on the island of Pulau Laut in South Kalimantan. This project is associated with various problems that have, so far, been largely ignored by the relevant authorities. These include:

Community issues: There is a real risk of community conflict as a result of the wood chip plant development. Very little information has been made publicly available by the Government authorities or the company. The inevitable result is a breakdown in trust within the community.

Environmental issues: Deforestation in South Kalimantan is already a serious issue. The few areas where natural forest remains, such as the Meratus mountains and Mt Sebatung, are suffering from illegal logging. Natural disasters, including landslides and floods, have become an annual event in South Kalimantan as the land cannot absorb the high rainfall.

Plantations: Pulpwood production from large-scale industrial tree plantations (*HTI*) in Indonesia has been low, partly due to the lack of investment and funding from the Reforestation Fund since the 1997 financial

crash. This is particularly so for most HTI in South Kalimantan. Furthermore, UFS has been in a long-running dispute with the Indonesian Forestry Department over ownership of the PT Hutan Rimba Banua plantation concession. The company's claims that plantations will feed its wood chip and a pulp plants it is planning to build at Satui, on the coast of South Kalimantan are not realistic, especially since UFS is trying to buy and operate the Kiani Kertas pulp mill in East Kalimantan. UFS' inability to provide data on the potential source of timber supplies for these three ventures indicates the likelihood that natural forests in South Kalimantan and further afield will be destroyed - legally or illegally to meet their needs.

The paper pulp industry is a major factor driving one of the highest deforestation rates in the world in Indonesia. The country's forests the third largest in the world are disappearing at over 2.8 million hectares/year. They provide and protect the livelihoods of tens of millions of rural and indigenous people, in addition to having high biodiversity. Some 70% of logging is illegal, but large tracts of natural forest are cleared legally to make way for pulpwood plantations which cause ecological and social problems. The Indonesian government has made many public commitments nationally and internationally to restructure Indonesia's wood processing industry and eliminate illegal logging.

Conclusions & key recommendations:

There should be an immediate independent review of the sustainability of timber supplies for all UFS's



Mangrove are in Pulau Laut

DTE

developments. UFS must, as a matter of priority, work on mitigating the environmental and social impacts of its Alle-Alle chip mill and no permit should be issued for the Satui pulp project.

In South Kalimantan, local economic development should focus on sustainable community-based forestry operations, not large-scale pulpwood plantations and woodchip or pulp mills. Local communities must be involved in decision-making about forest resources. Indigenous communities' prior, informed consent can only be freely given if people have access to information and help to interpret this before decisions are made (the FPIC principle); this means

more transparency of information from companies like UFS and government authorities.

More generally, all Indonesian wood chip and pulp plants should be required to prove that their sources of timber are legal and genuinely sustainable. No new permits should be granted by central or local governments to any pulp companies in Indonesia until independent surveys show that this is the case. Foreign investors; equipment suppliers; engineering, forestry and risk consultants should screen carefully for sustainability and not invest in projects in Indonesia likely to cause serious environmental damage, rights violations or social conflict such as those of UFS in South Kalimantan.

Table 2: Data on UFS Projects

Area of PT MHB/HRB plantation concession permit	268,585 ha ¹
Area of PT MHB plantation concession (actual)	259,000 ha ²
Area of PT HRB plantation planted by 2004	58,896 ha ³
Area of PT HRB plantation in good condition by 2005	15,000 ha ⁴
Area of natural forest remaining in PT HRB concession	73,060 ha ⁵
Area of concessions overlapping with PT HRB	87,000 ha ⁶
Maximum plantable area of PT HRB concession	93,566 ha (Table 4)
Area of PT MAL chip plant and harbour	88,216 ha ⁷
Production capacity of PT MAL chip mill	700,000 t/yr ⁸
Area of acacia plantation needed to supply PT MAL chip plant	85,895 ha (calculation on page 12)
Area of PT MBBM pulp plant (planned)	1,294 ha ⁹
Production capacity of PT pulp plant (planned)	600,000 t/yr ¹⁰
Production capacity of PT MBBM pulp plant (current)	525,000 t/yr ¹¹
Area of acacia plantation needed to supply PT MBBM pulp plant	206,667 ha ¹²
	258,333 ha ¹³
	203,437 ha ¹⁴
Total area of acacia plantation needed to supply UFS projects	629,783 ha ¹⁵

Sources:

- | | |
|--|---|
| 1 Forestry Department, 2005 | 9 PT Marga Buana Bumi Mulia, 2003 |
| 2 Jaakko Pöyry, 2004 (after concession maps re-measured) | 10 <i>ibid</i> |
| 3 <i>ibid</i> | 11 Ardi Y, 25 January 2005 |
| 4 pers com, protected source | 12 Jaakko Pöyry, 2004 |
| 5 Jurgens <i>et al</i> , CIFOR 2005 | 13 Global 2000, p27/2 |
| 6 Walhi South Kalimantan, 2002 | 14 Mid-point of JP and Global 2000's figures |
| 7 PT Mangium Anugerah Lestari, May 2005 | 15 Areas for Alle-Alle, Satui and Kiani Kertas added together |
| 8 UFS, Annual Report 2005 | |

A

INTRODUCTION



Tanjung Segi lighthouse, Alle-Alle village, Pulau Laut

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PT Marga Buana Mulia (PT MBBM), a company now owned by UFS, has had plans for a paper pulp mill in South Kalimantan since 1996. Indonesia's Department of Forestry blocked this project during a battle to reclaim state funding from the PT Hutan Rindang Banua (PT HRB) pulpwood plantation - also part of UFS - intended to supply the plant.

UFS says that its wood chip and paper pulp plants will be supplied from industrial timber estates (HTI) owned by the company, plus other plantations in South Kalimantan. However, timber plantation development has been very slow - hence concerns that these mills will lead to more natural forest destruction. Another issue is that neither the provincial and district level authorities nor the company has sought the free, prior and informed consent (FPIC) of indigenous communities likely to be affected by the projects.

Several foreign companies have been involved in the chip and pulp mill start-ups, ranging from equipment providers to forestry consultants. National and international non-governmental organisations (NGOs) strongly oppose their involvement.

At the time of writing, UFS was preparing to take over PT Kiani Kertas in East Kalimantan, even though the company has no experience in running pulp mills.

This report was originally compiled in Bahasa Indonesia, based on interviews with civil society organisations (CSOs) in South Kalimantan - such as Walhi South Kalimantan, LPMA Borneo Selatan, LSM Rindang Banua, the people of Tanjung Seloka and Alle-Alle villages, South Kalimantan and Kotabaru district authorities, PT HRB and MBBM. It also draws on field data from local CSOs and the author's seven years' advocacy experience in South Kalimantan.

It is intended to provide information to researchers and activists concerned with social and environmental issues, especially those who support the indigenous peoples' movement and who oppose the development of a paper and pulp industry that lacks social and environmental justice.

United Fiber System Ltd (UFS or UniFiber), a Singapore-based construction and property company, is currently building a wood chip mill¹ at Alle-Alle village in Kotabaru district, Pulau Laut, (lit. Sea Island) off the southeast coast of Indonesian Borneo.

¹ More information on wood chip mills is given in Box 3

B

FROM MHB TO UFS



South Kalimantan is the smallest Indonesian province on the island of Borneo, but has a wealth of forest and other natural resources. Forestry and mining companies are keen to get their hands on its tropical rainforests.

A variety of stakeholders in the forestry sector have watched with interest the development of the pulpwood plantation company originally called PT Menara Hutan Buana (MHB).

The company was established on 22 December 1994 as a joint venture between PT Wonogung Jinawi (60%), owned by Probosutedjo (ex-president Soeharto's half-brother) and PT Inhutani II (40%), a state-owned forestry company².

PT MHB was granted a 268,585 hectare timber plantation concession (*Hak Pengusahaan Hutan Tanaman Industri, HTI*) in South Kalimantan, by the Minister of Forestry on 27 February 1998, to supply the paper pulp industry (Decree No. 196/KPTS-II/1998³).

The concession covers the sub-districts of Riam Kiwa in Banjar district (37,835 ha); Kintap (83,000 ha) and Sebanban (65,000 ha) in Tanah Laut district; and Teluk Kepayang (62,500 ha) and Pamukan (20,250 ha) in Kotabaru district⁴ - an area about the size of Luxembourg or four times Singapore.

In December 2000, Inhutani II agreed to sell its shares to Wonogung Jinawi for Rp44 billion⁵ (US\$4.4 million). A year later, on 19 March 2001, all PT MHB's assets were taken over by foreign investors - PT Anrof Singapore Limited (ASL) and PT Shinning Spring Resources (SSR) Ltd - and eventually transferred to Singapore-based United Fiber System (UFS) (see Box 1).

Shortly afterwards (2 July 2002), the Indonesian Ministry of Justice and Human Rights authorised the company to register under the new name of PT Hutan

Rindang Banua (HRB) (Decree No. C-11987 HT.04.TH.2002).

In November 2002 the forestry minister publicly announced that the permits of 14 HTI concessionaires, including PT HRB, had been cancelled⁶. Ministerial decree No. 987/KPTS-II/2002, issued on 24 October 2002, revoked the permit previously issued to PT Menara Hutan Buana. The reason given was that company ownership had been transferred without prior written consent from the forestry department - even though PT HRB was still considered to be technically and financially sound⁷.

An additional reason was that PT MHB inflated its figures on the area planted with acacia in order to get more money from the Reforestation Fund (*DR*). So the Department of Forestry (representing the Republic of Indonesia) demanded that PT MHB/HRB returned the excess funding it received.

This caused a 'stand-off': UFS claimed the company could only afford to repay the Reforestation Fund loan from the proceeds of logging the PT HRB plantation concession. However, it is illegal to log without a permit and the Department of Forestry would only re-issue that once the company had paid its dues.

According to PT MHB, during 1994-1995 and 1996-1997, the company replanted an area of 71,024 ha with acacia. This did not match the findings of a survey carried out by a team representing the forestry department, anti-corruption agency (*BPKP*), state-owned forestry companies (PT Inhutani) and land survey co-ordinating agency (*Bakorsurtanal*) in June 2001 which found that only 41,212 ha had been replanted. By these figures, PT MHB should only have received Rp95.4 bn (US\$9.5 million), instead of the Rp144.4 bn (US\$14.4 million) it had claimed. This mark up cost the state Rp49 bn (US\$4.9 million) in public funds⁸.

² Kompas, 12 March 2001

³ Forestry Department, 2005

⁴ Walhi South Kalimantan, 2002

⁵ Kompas, op cit

⁶ Banjarmasin Post, 14 November 2002

⁷ Radar Banjar, 20 December 2002

⁸ Kompas, op cit

Different sources of information cite different figures for the area replanted by PT MHB/HRB. One local newspaper in South Kalimantan puts it at 44,335 ha⁹, while a national daily quotes the *Bakorsortanal* estimate of 41,212 ha¹⁰.

PT MHB says the company planted 75,758.43 ha between 1994/1995 and 1998/1999¹¹. This is close to estimates of 78,571 ha by the South Central Kalimantan Production Forest Project (SCKPFP).

UFS' forestry consultant, Jaakko Pöyry, states that the replanted area was 60,601 ha in 2000, and fell to 58,896 ha in 2004¹². It estimates that, by 2007, the replanted area will have shrunk further to 58,307 ha due to external factors, including logging by the local

community and overlapping concession permits (see Table 4).

However, field data from Walhi South Kalimantan indicates that, although the company may have replanted tens of thousands of hectares with acacia, only 15,000 ha are in good enough condition to be called an industrial timber estate¹³.

⁹ Banjarmasin Post, op cit

¹⁰ Kompas, op cit

¹¹ PT Marga Buana Bumi Mulia, 2003

¹² Jaakko Pöyry, 2004

¹³

BOX I

UNITED FIBER SYSTEM

United Fiber System (UFS) was created when the Singaporean construction company, Poh Lian Holdings Limited, took over Anrof Singapore Ltd (ASL) in April 2002.

ASL is a Mauritius-listed holding company. It held 100% of PT HRB and PT MBBM's shares either directly or indirectly through its subsidiary, Shinning Resources Ltd (SSR), registered in the British Virgin Islands. After the takeover, Poh Lian changed its name to United Fiber System to reflect its new businesses.

Tektronix Industries Ltd, also registered in the British Virgin Islands but owned by individual shareholders from Scandinavia, used to be ASL's majority shareholder. Since the takeover, Tektronix still owns 51% of UFS. Tektronix's owners are directors or managers of CellMark, a Swedish paper marketing company (see Appendix I).

UFS is listed on the Singapore stock exchange as a public company with net assets of S\$527,661,000 (US\$330 million). It now has two main divisions: forestry & pulp and construction & property. UFS' forestry & pulp division holds the permits for the 268,585 ha industrial timber estate and a pulp mill. It intends that the pulpwood will come from the PT HRB plantation. UFS' auditors list S\$339,000 (US\$212,000) of 'forest assets'.

The forestry & pulp division has added a further production unit - the chip mill. On 26 September 2003, UFS publicly announced it had set up a new company in Indonesia called PT Mangium Anugerah Lestari (PT MAL) as a subsidiary of its

Mauritius-registered Pacificwood Investment Ltd (itself a subsidiary of SSR Ltd).

In June 2005, UFS also announced its intention to take over PT Kiani Kertas in East Kalimantan, with Deutsche Bank leading a consortium of investors. UFS said the deal would give it a ready-made pulp mill and another source of revenue.

Deutsche Bank eventually withdrew from the scheme in January 2006 after pressure from international NGOs, Robin Wood, Rettet den Regenwald and Global 2000 (Friends of the Earth Austria).

This did not, however, end UFS' hopes of becoming a major player in Indonesia's pulp industry. The company is currently actively seeking backing for its investments in Kalimantan's forestry, pulp and woodchip sector. When this report went to print, UFS was on the brink of buying Kiani Kertas with a US\$2,500,000 loan from Cornell Capital Partners, an American investment company.

Sources:

- Jurgens et al, 2005
- UFS website, www.ufs.com.sg
- UFS, 26 Sept 2003
- UFS, 2004
- UFS, 2005
- Financial Times.com, 4 July 2005
- Zabao.com, 28 August 2005
- Insinyur Kimia Online, 16 August 2005
- WRM Bulletin, January 2006
- Bisnis Indonesia, 14 February 2006

The majority of the concession area had been cleared of rainforest even before the forestry department issued the original permit for PT MHB/HRB. Some of the forest destruction was recent: the Pamukan sector was zoned for selective logging (*HPH*) until 1997. It is not clear how its status changed to become an industrial tree plantation (*HTI*). Although many parts have been invaded by elephant grass (*Imperata cylindrica*), a substantial amount of natural forest remains: 73,060 ha¹⁴.

Of the 268,585 ha covered by the PT HRB concession, approximately 87,000 ha¹⁵ overlaps with other concessions, including the coal mining company, PT Arutmin, and an oil palm plantation planned for Kotabaru district under a permit issued by the district head (*bupati*). PT HRB has not delineated the new plantation boundaries so, by early 2006, the total useable area of the concession remains unclear.

After the forestry minister revoked PT HRB's permit, the company took the case to the state administrative court (*PTUN*) in Jakarta, asking for the decree to be invalidated. PT HRB won the first round. The court declared that the forestry department had to postpone implementation of its October 2002 decree withdrawing the PT MHB/HRB permit (Verdict No. 209/G.TUN/2002/PUTB-Jkt)¹⁶. The forestry department appealed against this decision and the case went to the Indonesian Supreme Court¹⁷.

In October 2005, (then) UFS Chief Executive Officer, Kishore Dass, announced to the Singapore Stock Exchange that the Supreme Court had decided in favour

¹⁴ Jurgens et al, CIFOR 2005

¹⁵ Walhi South Kalimantan, 2002

¹⁶ Radar Banjar, op cit

¹⁷ Antara, 25 August 2005

BOX 2

JAAKKO PÖYRY

Jaakko Pöyry (JP) is a Finnish forestry consultancy involved in all aspects of Indonesia's timber plantation sector. Set up in 1958, JP is a now a consultant for the pulp and paper industry world-wide with offices in 25 countries, including Sweden, UK, France, Germany, Netherlands, Spain, Portugal, Russia, Brazil, Argentina, Chile, Thailand, Indonesia, Australia, New Zealand and the US.

JP's first involvement in global forest destruction started in 1978, with the giant Aracruz Celulose project in Brazil, one of the world's biggest pulp producers. It has helped Aracruz expand its eucalyptus pulp production to 2.8 million tonnes per year by 2005.

Jaakko Pöyry has become a major driving force in shifting the production of wood fibre - the main raw material for making pulp - from the North to the South. Timber grows much faster in tropical countries than in temperate zones. Moreover, there is cheap land, low wages and lax environmental and social control in many southern countries. Not surprisingly, Indonesia is the world's cheapest paper pulp source.

In 1984 Jaakko Pöyry was contracted by the World Bank to carry out a study of Indonesia's

forestry sector. Four years later, the Asian Development Bank and Indonesian government asked the company to study the potential of the pulp and paper industry in the country.

As a result, Jaakko Pöyry secured over 30 contracts in Indonesia to plan or implement projects to supply the pulp industry, using natural forests or pulpwood plantations. The company has been involved in all Indonesia's controversial pulp and paper developments, including Indorayon/Toba Pulp Lestari and Riau Andalan and now the Satui pulp plant plan. The company has also been a broker for equipment supplies to these factories.

Observations of pulpwood plantation and paper pulp projects in Indonesia show that JP studies have resulted in forest destruction and land rights violations with no compensation for communities.

Currently, JP is the consultant for the pulp and chip mill developments in South Kalimantan. It has conducted a raw materials study for UFS' projects, but the results failed to convince local, national and international NGOs that UFS can source its raw materials from plantations rather than from natural forests.

In response to this opposition, UFS asked JP

of the company¹⁸. UFS now regards the case as over, and told its shareholders that it “allows us to continue our forest plantation activities to ensure a sustainable supply of wood to our planned pulp mill”¹⁹.

The Supreme Court's decision means that PT HRB can once again legally log within its plantation concession, harvesting acacia and - if it so chooses - natural forest. Forestry minister M. S. Kaban has so far still refused to reissue a license to the plantation company²⁰. But, whatever his opinion of the court verdict, PT HRB now has the legal right to resume operations based on the permit originally issued to its forerunner, PT MHB.

Kaban is very keen to increase the forest sector's contribution to local and national revenues, and pulp and paper development is an important part of this. Also, MIGA is consulting with UFS/HRB on the management of the plantation, increasing the likelihood that both the chip and pulp plants will go ahead quickly.

So this legal battle will probably now be quietly forgotten.

From the start, the PT MHB/HRB plantations were intended to supply the main raw material timber - to the paper pulp mill to be developed by PT Marga Buana Bumi Mulia (MBBM). This company, now also a UFS subsidiary, was established on 19 September 1996²¹ to set up and run a bleached hardwood kraft pulp (BHKP) mill in South Kalimantan²². It aims, initially, to produce up to 600,000 tonnes per year of elemental chlorine-free (ECF) pulp from supplies of *Acacia mangium*²³.

¹⁸ Ardi Y, 1 December 2005

¹⁹ UFS, Annual Report 2005

²⁰ Tempo Interaktif, 1 December 2005

²¹ Jurgens et al, op cit

²² UFS Pulp Division

²³ PT Marga Buana Bumi Mulia, 2003

- assisted by an independent consultant with public relations expertise - to meet some of the NGOs.

The NGOs they wanted to meet on their short trip to Indonesia in March 2006 included TELAPAK, Forest Watch Indonesia (FWI), Walhi's National Executive (Friends of the Earth Indonesia), Walhi South Kalimantan, Community Alliance for Pulp and Paper Advocacy (CAPP), Indonesian Ecolabeling Institute (LEI), SKEPHI, Conservation International (CI), TNC, CIFOR, WWF and Rainforest Alliance (Smartwood).

CAPP, Walhi's national office and Walhi South Kalimantan felt the meeting with JP would be pointless without a decision-maker from UFS. As JP did not meet this request, none of these NGOs took part.

In a meeting at TELAPAK's office on March 3rd 2006, JP - represented by Maree Candish, Eulen Chew and Jonathan Wootliff - explained that the purpose of meeting the Indonesian NGOs was to:

- help UFS to understand Indonesian civil society which, it felt, had raised more complex issues than international NGOs;
- help UFS identify which groups would help them

to understand local problems; and

- understand which issues UFS should focus on in dialogues with civil society.

They also wanted to be recommended to NGOs that understood UFS' position and could inform the company about what Indonesian NGOs wanted.

However, JP only seemed interested in collecting information about NGO objections to the South Kalimantan pulp and wood chip mill plans. It gave no information about UFS or where it would source its raw materials. JP said it didn't have this information although, as UFS' forestry consultant, it must have known. Clearly UFS and its consultant do not want to reveal their hand to NGOs and the Indonesian public.

Sources:

- Jaakko Pöyry, 1995
- Hidayati, N et al, 2005
- Notes of meeting with Jaakko Pöyry, 3 March 2006
- Carrere, R & Lohmann L, 1996
- CAPP email to JP, 28 February 2006



Sign for PT MAL's project at Alle-Alle

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The plan is to build the mill in the village of Sungai Cuka in Satui sub-district, Tanah Bumbu on the south-east coast of the province. It will cover an area of 1,294.404 ha, of which 454.15 ha will be for factory buildings, plus a buffer zone and town site²⁴.

Since last year's Supreme Court verdict, UFS has been planning to start preconstruction work on the Satui pulp mill as soon as its purchase of Kiani Kertas goes through. Start up has been rescheduled for 2009²⁵.

Meanwhile, UFS had created a new subsidiary called PT Mangium Anugerah Lestari (PT MAL). On 22

April 2003, UFS' chairman announced plans to set up a US\$39 million wood chip mill²⁶. On 24 December 2004, the Singapore branch of Raiffeissen Zentralbank Österreich AG (RZB-Austria) agreed to provide a US\$21 million loan for the project to complement the US\$18 million granted by China National Machinery and Equipment Import & Export Corporation (CMEC). Some equipment will be provided by the Austrian company, Andritz AG²⁷. The chip mill project began in August 2005, with land clearance.

The contract states that the South Kalimantan wood chip mill will have a production capacity of 700,000 *bone dry metric tonnes* (bdt) per year. Estimated costs had increased by 2006 to US\$45 million. The financing, construction of the plant and its port plus the equipment supplied by CMEC were all underway when this report went to press²⁸.

²⁴ Ibid

²⁵ UFS, Annual Report 2005

²⁶ UFS, 22 April 2003

²⁷ UFS, 24 December 2004

²⁸ UFS, Annual Report 2005

Table 3: South Kalimantan data

Area	3,7 million ha	South Kalimantan Province website
Population (2000 census)	2.985.240	Indonesia Statistic Agency
Area of forest cover (actual)	1.138.500 ha	Indonesian Department of Forestry, 2005
Protected Forest (National Park etc)	85.700 ha	
Protection (watersheds)	367.800 ha	
Production (selective logging)	645.000 ha	
Conversion (clear felling)	40.000 ha	
Area of active logging concession (HPH)	320.531 ha	Direktorat Jenderal Bina Produksi Kehutanan, August 2005
Area of Industrial Forest concession (HTI)	252.365 ha	Direktorat Jenderal Bina Produksi Kehutanan, June 2005
Official forest area 1999	1.839.000 ha	Indonesian Department of Forestry, 2003
Annual deforestation rate	3,8 %	Indonesian Department of Forestry, 2003
Annual of critical land	556.000 ha	Kompas, 22 February 2006

WOOD CHIP MILLS IN OTHER COUNTRIES

Chip mills process timber - trees or parts of trees - to produce wood chips which are then used to feed pulp and paper mills. The industry does not practice selective logging - it uses whatever timber it can as the raw material; almost any species will do.

Wood chip mills convert timber into small chips in a matter of seconds. This huge wood processing capacity can become a driving factor in the aggressive expansion of large-scale logging operations. Such mills can convert trees of any size into wood chips 2-5 cm long. Most parts of the tree - from the trunk down to branches as small as 7cm in diameter - can be turned into chips, completely destroying forests and everything that lives in them.

Fast-growing tree species, such as pine, eucalyptus or acacia, may be planted after natural (mixed hardwood) forests are clear-felled. However, studies show that 95% of biodiversity is lost after conversion to timber plantations. The flora and fauna need the diversity of tree species found in natural forests in order to survive, not fast-growing monocultures.

Almost all wood chip mill operations (after the initial logging) are mechanised. So, as in the paper pulp industry, the employment potential is low.

In some places, such as southern states in the US, chip mills are seen as extremely harmful consumers of natural forests which fuel deforestation. In Georgia, for example, more than 130,000 acres of forests are clear felled each year to feed 13 chip mills operating in the state.

In 1998, the Blue Ridge Environmental Defense League (BREDL) asked the US Deputy

President to impose a moratorium on 18 chip mills in North Carolina, which were using 4.5 million tonnes of wood and destroying 123,000 acres of forest every year. In 2000, the people of Tennessee in the southern US also demanded a chip mill moratorium; in their state there were 156, consuming 1.2 million acres of forest per year.

In Australia and the Philippines, some 5 million m³ of forest timber is being converted to wood chips annually, mainly for export to Japan. Greenpeace is actively campaigning against wood chip mills in Tasmania, where large-scale logging to feed chip mills is clearing old growth forests.

Tropical hardwood chips sell for US\$120-130/tonne on the world market and there are plenty of buyers in the paper pulp sector.

The impact of the chip mill industry is not limited to the destruction of forests or the livelihoods of communities living in and around forests. For people living near such mills there are other negative aspects, such as noise and dust pollution, the dangers of large trucks using village roads to access the mills, the devaluation of land and property and reduced water quality.

Sources:

- Tribune Online News Story, 21 May 2000
- Practitioner, November 1997
- BREDL, 5 August 1998
- Dogwood Alliance
- tasmaniantimes.com, 28 June 2005

Note: 1 acre = 0.4047 hectares

C

FORESTS IN DANGER

News of the plans to set up a paper pulp mill in South Kalimantan spread after the provincial governor for 2000 - 2005, Sjachriel Darham, returned from a trip to Expo 2000, in Hannover, Germany.

The governor used that opportunity to get investment commitments totalling US\$3,340 million. The largest (US\$1,200 million) was for PT MBBM to set up a pulp mill with a production capacity of 600,000 tonnes per year in the districts of Kotabaru and Tanah Laut. Local newspapers reported that a consortium of companies from eight different countries was behind the deal - the Netherlands, Austria, Finland, France, Sweden, US, China and Singapore.

Work on the pulp mill was initially scheduled to begin in mid 2003²⁹ but, due to delays issuing the necessary permits, it was 14 August 2003 when the governor of South Kalimantan officially endorsed the

project. Local authorities and embassy delegates from the other countries involved witnessed the announcement at a celebration of the province's establishment³⁰. However there are no signs yet of a paper pulp mill on the ground.

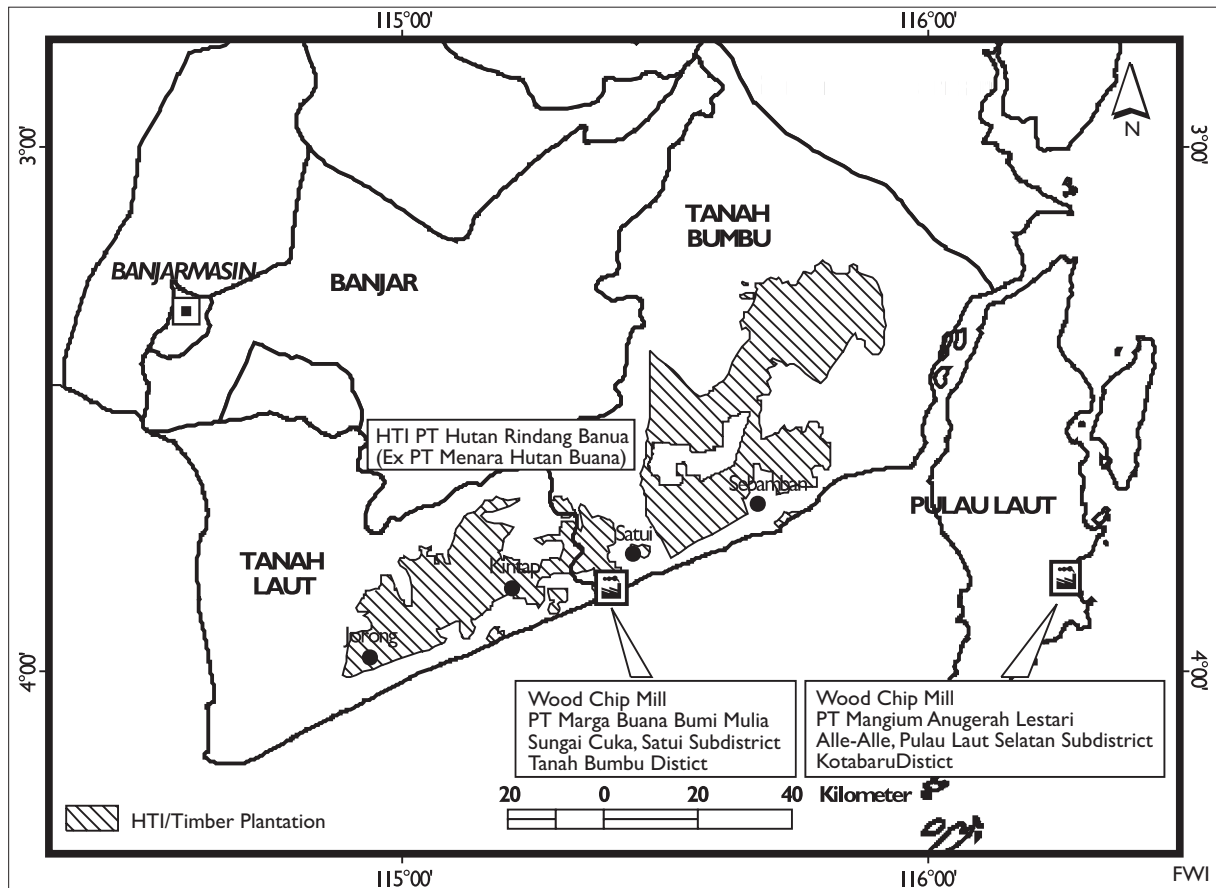
The main problem for PT MBBM's operations has been the dispute between PT HRB and the forestry department over withdrawal of its HTI permit. PT MBBM could do little faced with uncertainties over the legality of what was supposed to be its main feeder plantation. Moreover, the Indonesian government requires companies who plan to set up pulp mills to establish their own plantations³¹.

²⁹ Radar Banjar, 20 December 2002

³⁰ Radar Banjar, 15 August 2003

³¹ AgroIndonesia.com, 25 July 2005

MAP 2: PT HRB's Industrial Timber Plantations



Lack of certainty about permits and supplies has not affected the PT Mangium Anugerah Lestari (PT MAL) wood chip mill. At present, the only official permit that PT MAL possesses is from the local administrator - the *bupati* of Kotabaru district. Entitled "Permit Extension for the Land needed to set up an integrated Chip Mill and Port" (No.14/P/2004), this decree covers 88.216 ha in the villages of Alle-Alle and Tanjung Seloka in the south of Pulau Laut³².

In theory, the PT MAL wood chip mill will be supplied with timber from three local HTI concessions: PT HRB, PT Inhutani II and PT Inhutani III. In practice this is unrealistic. PT HRB does not have sufficient acacia ready to harvest, and PT Inhutani II and III currently supply timber to the Kiani Kertas pulp plant in East Kalimantan (see Appendix 3).

In addition, PT HRB's concession area has been significantly reduced by overlap with concessions granted to other companies. In addition, the Kintap, Sebamban and Satui blocks are not suitable for plantation development because they contain settlements.

Meanwhile, local authorities prefer to prioritise land use permits for oil palm plantations, which they believe will generate profits faster than timber plantations. Where concession permits overlap, existing pulpwood plantations may only remain until harvested. After clearing, the land will be taken over by oil palm plantation companies which have been granted permits (HGU). The area between Kintap and Sungai

Danau has already been converted to oil palm plantations.

Unofficial local initiatives further reduce the effective area of the PT HRB plantation. During a joint field trip, Walhi South Kalimantan and Global 2000 (Friends of the Earth Austria) were told that the head of Sebamban village had reclaimed land previously rented to PT HRB for its plantation and allowed villagers to fell the acacia trees if they needed timber to build houses.

PT HRB's concession area overlaps with eleven oil palm plantations concessions, a coal mine owned by PT Arutmin and sites used unofficially by local people for mining (*peti*). The oil palm plantations are operated by the following companies: PT Damit Mitra Sekawan and PT PKIS in Jorong; PT Pola Kahuripan Inti Sawit (PKIS) and PT SMART in Kintap; PT Damit Mitra Sekawan and PT SMART in Satui, PT Sayang Elang and PT Rumpun Subur Abadi in Sebamban (both subsidiaries of the same Malaysian group), PT Alam Raya Kencana Mas in Pamukan, PT Singalen in Teluk Kepayan, and PT Gawi Makmur Kalimantan (GMK) in Sekapuk.

PT HRB and PT Arutmin reached an agreement over their overlapping concession areas some time ago. They agreed that PT Arutmin would only mine where PT HRB had yet to plant trees or in plots with trees at least five years old. Although wood is usually harvested after

³² PT Mangium Anugerah Lestari, May 2005

Table 4: Estimate of area required for South Kalimantan pulp project supply

Description	Estimated area (ha)				
	2000	2004	2005	2006	2007
PT HRB plantation concession area	259,000	259,000			58,307
Area already planted	60,601	58,896		58,307	
Areas of <i>alang-alang</i> grass/scrub that can be used		35,615		35,259	
Maximum area that can be planted		94,511		93,566	6,485
Natural forest in the Pamukan area of the concession that will not be used	36,000	36,000			
Possible fibre sources from other HTI plantations		6,057			
HTI plantation concession area which has not yet been planted and can be used		113,550			
Possible expansion of HTI concession				3,000	9,000

Source: Jaakko Pöyry, November 2004

six years, PT HRB was prepared to harvest plots overlapping with the mining concession sooner. If PT Arutmin mines areas planted with trees under five years old, it has to pay PT HRB compensation³³.

PT Arutmin is currently mining such areas within PT HRB's concession - having given the company one year's notice of its plans. However, PT HRB was unable to harvest the wood while awaiting the outcome of its litigation against the forestry minister.

Forestry consultants, Jaakko Pöyry, have been highly optimistic about the supplies of pulpwood from PT HRB (see Table 4). Its own figures show that, of the

295,000 ha concession, the total area UFS can exploit is 93,566 ha at most³⁴ due to overlapping concessions and encroachment. Even the 75,758.43 ha cited in MBBM's environmental impact assessment report (AMDAL) is a huge over-estimate. By 2005, UFS stated that "an independent review of the plantation area showed a declineto 46,000 ha"³⁵. Currently, there may be as

³³ Personal communication by secured source

³⁴ Jaakko Pöyry, 2004

³⁵ UFS, Annual Report 2005, p66

BOX 4

INDUSTRIAL TREE PLANTATIONS A FLAWED POLICY

Indonesia is one of the world's lowest cost producers of paper pulp. However, its pulp and paper industry runs on a huge financial and ecological debt. Industrial wood plantations (*Hutan Tanaman Industri, HTI*), intended to supply the pulp mills, are part of this story of unstainability.

Indonesia's deforestation rate has averaged 2.8 million hectares per year since 1996. The pulp and paper industry has been a major cause of forest destruction. In 2000, pulp production required 23-25 million m³ of wood, while timber plantations could only supply 3.8 million m³. So, 85% of the timber demand for the pulp industry was met by clearing natural forests. Much of this forest was in areas zoned for conversion into HTI concessions.

Although clearly responsible for forest destruction, the pulp industry has been supported by the Indonesian government with credit, licences and other forms of assistance. For example, Indonesian pulp and paper producers had debts amounting to US\$17 billion in foreign currency after the 1997 financial crash, but no major company was forced to close. The Indonesian Bank Restructuring Agency (BPPN) allowed the same managements to continue. Despite this, president Susilo Bambang Yudhoyono wants the Reforestation Fund (DR) - a levy collected from logging companies - to finance a new drive to develop HTI plantations.

The government has set an initial target to develop 5 million hectares of HTI plantations by 2009. It will also speed up licensing and relax regulations considered to hamper the process, then invite investors to develop HTI plantations in Indonesia.

This is not the first time that HTI companies have benefited from the Reforestation Fund as a form of development assistance. Presidential Decree No.29/1990 extended an earlier decree on the Reforestation Fund (No. 32/1998) which initially allocated soft loans for reforestation logged-over forest areas. The new decree allowed the Fund to be used for HTI projects.

Many Reforestation Fund loans to HTI companies became bad debts which are still outstanding. In 2004, the forestry department rescheduled Reforestation Fund loans for HTI projects; 14 HTI companies closed because they could not pay up.

It is extraordinary that such an environmentally destructive industry, which has led to financial losses contributing to Indonesia's poverty, still benefits from funding support and other advantages in the name of generating state revenues and reducing poverty.

Sources:

- FWI/GFW, 2001
- Human Rights Watch, January 2003
- DTE Newsletter 48, February 2001
- IWGFF, 2004
- Forestry Department Press Release No:S.453/II/PIK-1/2004
- Tempolnteraktif.com, 13 April 2005
- Kompas, 16 June 2005
- AgroIndonesia.com, 21 June 2005
- <http://www.depkominfo.go.id>, 23 Mei 2006

little as 15,000 ha of PT HRB's concession with timber plantation in good condition³⁶.

It has been common practice in Indonesia for companies to apply for HTI concessions simply to exploit any commercially valuable natural forest within the area. A World Bank report predicts that Kalimantan's lowland forests will be commercially logged out by 2010³⁷.

Since 1999, few HTI concessionaires in South Kalimantan have carried out any replanting. The companies say this is due to their shortage of capital and lack of access to loans from the Reforestation Fund. The only exception is state-owned company, PT Inhutani II, which is currently replanting its logged over areas with acacia.

This situation presents a number of problems - not least, a serious shortage of acacia and other fastwoods from local plantations in the coming decade.

some 40,000 ha of forest in the north of Pulau Laut³⁸, but satellite images and field reports show no firm evidence of this (see Map 3).

Moreover, UFS has discussed plans for new access roads in South Kalimantan³⁹ (whether for the HTI concession, pulp mill or chip mill is not known). Wherever new roads are built through forests, forest destruction increases as they provide access to illegal loggers and farmers.

The threat that PT MAL's demand for timber poses to the forests of South Kalimantan is illustrated by the following figures and Table 5.

Between 4.5 and 5.4 m³ of logs are needed to produce one tonne of pulp for paper production⁴⁰. For one bone dry tonne of wood chips, 1.46 m³ of timber is needed. So PT MAL will need at least 1.02 million m³ of logs a year to meet the mill's 700,000 tonne capacity.

The average yield of Indonesian HTI estates is

Table 5: Timber demands of wood processing industries

Type of mill	Capacity	Timber consumption/y (cubic m RTE)	Equivalent Area HTI (ha)	Equivalent Area Natural Forest (ha)
PT MAL (Alle-Alle) chip mill	700,000	1.02 million	85,895	22,310
PT MBBM (Satui) pulp mill	600,000	2.79 million	195,300	50,727
PT Kiani Kertas (Mangkajang) pulp mill	525,000	2.44 million	170,800	44,364
TOTAL		6.25 million	451,995	117,401

So companies and communities will depend on felling natural forest to meet their timber needs.

The social and environmental costs of forest destruction, including loss of biodiversity, are high. Areas of natural forest or HTI which have been clear felled and left without replanting are vulnerable to soil erosion, especially in hilly regions, and quickly invaded by coarse grass (*alang-alang*). The Indonesian government calls the result 'critical land'. Local entrepreneurs may claim the land for speculation or - particularly in South Kalimantan - coal mining, while indigenous communities may reclaim ancestral lands for agriculture: both leading to conflicts with plantation companies.

Until UFS' timber supply problem is resolved by the increased availability of acacia from HTI plantations, it is likely that its companies will have to depend on destructive logging, illegal logging or both. Most obviously at risk are the 73,000 ha of forest within PT HRB's plantation concession and an unknown amount of forest on Pulau Laut. Jaakko Pöyry mentions

125 - 150 m³ per hectare over a 6-8 year cycle⁴¹. According to Jaakko Pöyry's research for UFS, PT HRB could achieve overall yields of 130 m³ timber per hectare on parts of its plantations where the acacia is over 11 years old. Allowing for 10% losses, these would deliver 117 m³/ha at the mill and would last for the first five years of operations⁴².

In fact, the actual planted area of PT HRB's concession is only 46,000 ha⁴³. Even if all this area had been planted with acacia 11 years ago and it were in

³⁶ LSM Rindang Banua, pers com

³⁷ Holmes, D., World Bank, 2000

³⁸ Jaakko Pöyry, 2005

³⁹ Jaakko Pöyry, October 2005

⁴⁰ Ibid, FWI/GFW, 2001

⁴¹ IWGFF, 2004

⁴² Jaakko Pöyry, 2004, op cit

⁴³ UFS, Annual Report 2005, p66

prime condition, it would only produce enough timber to run the chip mill for 5.3 years at full capacity or for 7.5 years production at 70% capacity.

Volume 1 ha planted estate (11 year old acacia): 117 m³
 46,000 ha planted estate clear felled: 5,382,000 m³

On average, the productivity of acacia on HTI estates in Kalimantan is 15 m³/ha/y. So for trees harvested at 7 years after planting, the total yield/ha is 105 m³ which, given losses during felling or transport (roughly 10%), translates as 95 m³/ha. Allowing for harvesting, improving the soil and replanting, this gives an 8 year cycle for a well-managed plantation.

The area of plantation required to supply the chip mill is estimated as follows:

Production capacity:	700,000t/year
or:	1,020,000 m ³ /year
Harvesting cycle:	8 years
Production capacity for 8 yrs:	8,160,000 m ³
Volume 1 ha planted estate:	95 m ³
Total estate area required:	85,895 ha
Estate area needed per year:	10,737 ha

Jaakko Pöyry reckons that, with improved varieties of acacia and better management techniques, annual growth increments of 25 m³/ha are possible for the HRB concession in the future⁴⁴. This highly optimistic figure far exceeds any achieved to date in the area.

Yet PT HRB's total plantable area is only 93,566 ha - unless it clears the forest remaining in its concession. Moreover, if it is true that the area of well managed timber plantation in PT HRB's concession is as low as 15,000 ha, there is obviously a substantial potential deficit⁴⁵. This is only enough for 1.5 years of the wood chip mill's operations.

So where might the rest of the timber for the wood chip mill come from? There are two likely scenarios. The first is based on field evidence that PT Inhutani II is the only concession holder currently replanting its estate. The second draws on data in PT MBBM's environmental impact assessment report (AMDAL) on local supply capacity.

Scenario 1

- PT HRB	: 15,000 ha
- PT Inhutani II	: 28,320 ha +
	43,320 ha

Scenario 2

- PT HRB	: 15,000 ha
- PT Kirana Khatulistiwa	: 4,100 ha
- PT Inhutani II	: 37,450 ha
- PT Inhutani III	: 20,200 ha +
	76,750 ha

As at least 85,895 ha are needed on an 8-year cycle, the shortfall for Scenario 1 is: 42,575 ha and for Scenario 2 is: 9,145 ha. Yet there is only an estimated 129,362 ha of acacia in South Kalimantan⁴⁶, outside PT HRB's 49,000 ha plantation (see Appendix 3). There is no information as to whether UFS has signed agreements with any other pulp wood plantations except Inhutani II. Also, some are said to be supplying timber to pulp mills in Sumatra. In short, there are not sufficient plantations for the chip mill to run at near capacity, so the raw material will be 'supplied' by natural forests.

UFS should explain how these figures are compatible with its statement that all its mills will exclusively use plantation wood and that high conservation forest will be spared⁴⁷.

Unless UFS operates very strict controls, timber from unknown outside sources may enter its chip or pulp mills. So PT MAL and PT MBBM could - knowingly or unknowingly - benefit from the results of illegal logging. The issue is not just illegal logging, but destructive logging. Now the court case has been settled in favour of PT HRB's licence, the company can legally clear natural forest in its own concession. Inhutani II already has permits to turn forest on Pulau Laut into HTI plantations.

Last year, UFS signed a contract with PT Inhutani II for 1 million tonnes of timber over three years⁴⁸, but this is not enough to keep Kiani Kertas in full production for 6 months. It is not clear which other local HTI concessions PT MAL plans to draw on for supplies of raw timber in addition to PT HRB. No other agreements seem to have been signed. If PT Inhutani II

⁴⁴ Jaakko Pöyry, 2004

⁴⁵ LSM Rindang Banua, pers com

⁴⁶ Jaakko Pöyry, 2004

⁴⁷ UFS, Annual Report 2005

⁴⁸ Sinar Harapan, 8 August 2005

and Inhutani III sell their logs to pulp mills in Riau or East Kalimantan, or decide to protect some of the natural forest in their concessions, then the South Kalimantan wood chip mill faces yet more serious problems in obtaining sustainable supplies.

Forestry Department data showed that, as of November 2005, not one final decree (SKD) had been issued allowing a HTI to be set up for pulp production in South Kalimantan⁴⁹. Despite this, UFS and its consultants still insist that its wood chip mill will be supplied only from sustainable sources rather than mature tropical forests.

As UFS is planning to build the PT MBBM pulp mill at Satui and is currently operating - and hopes to buy - the PT Kiani Kertas pulp mill in East Kalimantan, it is logical to expect that the wood chips produced at its

Alle-Alle plant will be supplying these. However, this is now in doubt. UFS signed a purchasing agreement with CMEC (China National Machinery and Equipment Import and Export Corporation) in May 2005. CMEC - currently building the chip mill on a 'turnkey' arrangement - will buy 90% of the chip mill production and have an option on the other 10%⁵⁰. Neither UFS' press release or its 2005 Annual Report gives any information about how long this agreement is to last. Unless UFS buys the wood chips back from CMEC (which seems uneconomic), this means that both Kiani

⁴⁹ Bina Produksi Kehutanan, via FWI, April 2006

⁵⁰ UFS website, press release, 28 April 2005

BOX 5

THREATENED: MERATUS FORESTS

The Meratus Mountains cover nine districts of South Kalimantan: Kotabaru, Tanah Bumbu, Tanah Laut, Banjar, Tapin, Hulu Sungai Selatan, Hulu Sungai Tengah, Hulu Sungai Utara and Balangan. There are around 300 *balai* in this forested region - the ancestral home of the Meratus Dayak people. The forest is essential to them; it forms the basis of their lives and is an integral part of their culture and religious beliefs.

The forests of the Meratus Mountains contain some giant, ancient trees and act as a water catchment area for South and Central Kalimantan provinces. When the logging industry took off in South Kalimantan, many of the largest specimens of meranti and ramin were felled to supply wood processing mills. People were given chainsaws to cut down their own trees. As a result, big trees - which harboured wild bees whose honey was collected at certain times of the year - became scarce in Meratus. Moreover, the trees needed to build *balai* and houses became increasingly hard to find.

The indigenous community split into two camps: one wanted to follow traditional knowledge systems to maintain the forest as a sustainable resource; the other believed they may as well benefit from the theft of their forest, if it was being destroyed anyway.

During several meetings with Meratus Dayak communities in the *balai* of Limbur Lokasi,

Libaru Baras and Gadang in Kotabaru district during 2004, people in this second group explained why they had participated in the destruction of their forests. They preferred to get some financial return, rather than just standing by while others profited from their timber. Reversing the old Indonesian proverb "Put up with tough times now to enjoy the benefits later", their philosophy was "Live now, pay later". If disaster followed, they would think about how to deal with it then.

However, local people get very little financial return for felling the forests. Usually, they are only employed to cut down trees, selling the timber to traders for Rp250,000 - 300,000 per m³. Transport costs and petrol for the chainsaw are deducted from this, so each person only earns Rp60,000 - 100,000 (US\$6-10) for a week's work. The logs are then taken to a wood processing mill elsewhere in the province.

Despite high levels of 'illegal logging' in South Kalimantan, only 145 cases were recorded by the South Kalimantan police in 2003. Most stolen timber is *meranti* or *ulin*, which has a higher commercial value than other wood species.

Sources:

- South Kalimantan police, 2003
- Field visit notes, *balai* Limbur, 2002-2004

Note: A *balai* is a small community unit within Meratus Dayak. It also means the community hall used for gatherings and/or living.

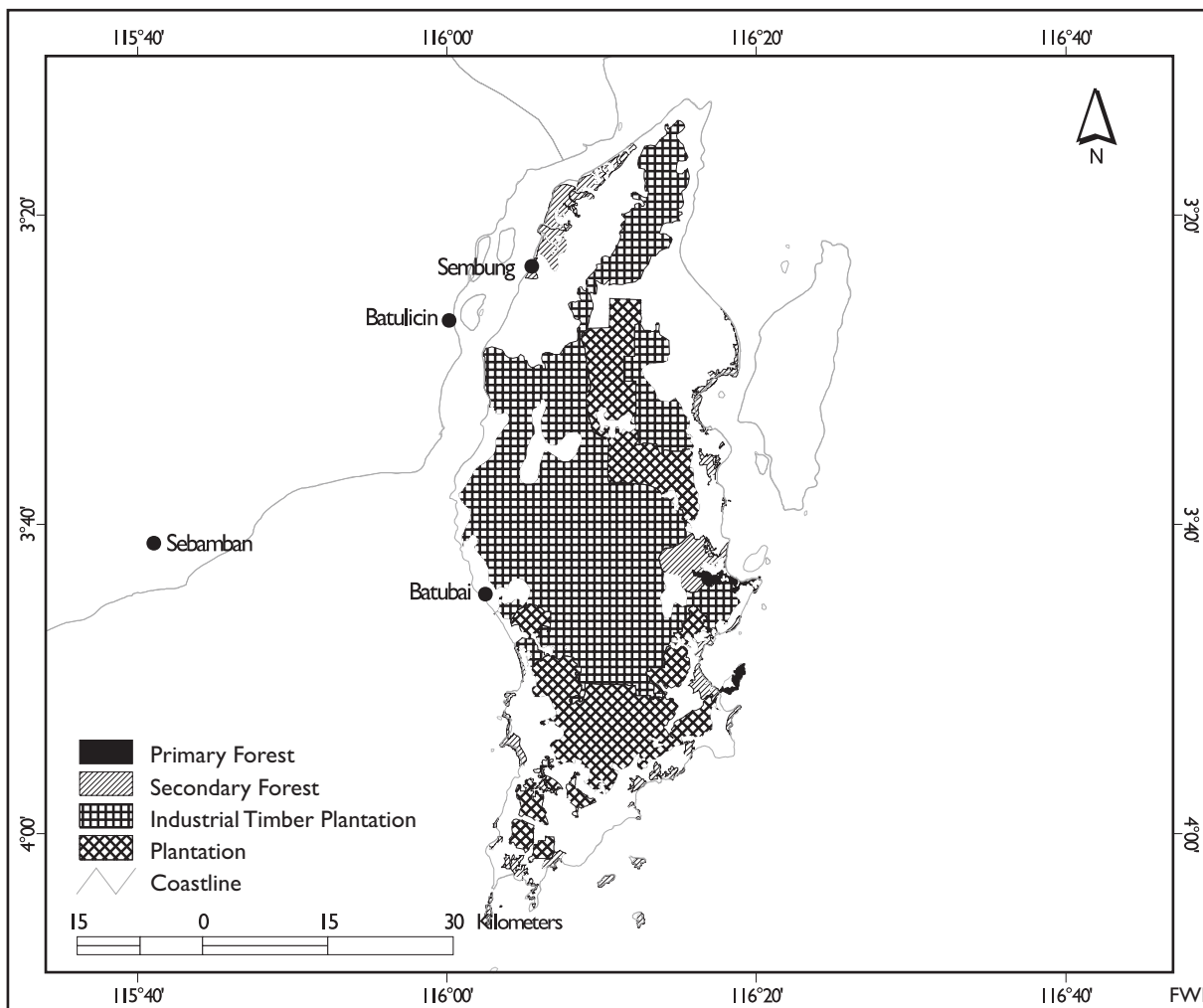
Kertas and the proposed Satui pulp mill will have no source of raw material from HRB, because nearly all the timber going into the chip mill from UFS' plantation - and others such as Inhutani II - will be exported, probably to China.

If the provincial authorities keep pushing for the establishment of the chip and paper mills in South Kalimantan, this will inevitably pose a severe threat to forest-dependent people in the province, especially the Meratus Dayak. A precedent was set back in 1999 when 46,000 ha of the Meratus mountains was reclassified specifically to give the Korean logging company PT Kodeco Timber access to commercially valuable timber in return for giving up a concession area near the coast⁵¹.

Apart from being the basis of the livelihoods of the indigenous Meratus Dayak, the forests covering the Meratus mountain range act as a water catchment system for the provinces of South and Central Kalimantan. As much of southern Borneo is at or below sea level, stripping the hillsides of forest can bring disastrous floods to the low lands where most of the population lives and farms. It is these forests that are now under threat (see Appendix 2).

⁵¹ DTE Newsletter 50:7, August 2001

MAP 3: Forest on Pulau Laut



D

MINIMAL TRANSPARENCY



Drying fish along the harbour at Tanjung Seloka

DTE

From the very start, UFS' policy has been to withhold crucial information about its operations in South Kalimantan - a lack of transparency supported by the provincial authorities. Yet people are entitled to information about plans to convert or exploit forest resources under Indonesian law. NGOs have had to rely on the media for information on the company's operations and its partners. Neither UFS nor the local authorities have undertaken steps to seek the free, prior informed consent of indigenous communities likely to be affected by the project, as required by international law.

All large new developments in Indonesia with likely environmental and social impacts have a statutory obligation to carry out an Environmental Impact Assessment (EIA/AMDAL). No work should start until this report has had a public hearing and been approved by Jakarta and the local authorities. It is not known when or where the public meetings were held to discuss the

EIA for UFS' Satui pulp mill or its chip mill on Pulau Laut. Local CSOs were not invited and have not been able to obtain copies of the relevant documents for PT MAL. Furthermore, there is no information on UFS' website about the EIAs, management plans or the permits needed to establish and operate the pulp or chip mills.

UFS told Jaakko Pöyry in 2005 that an 'AMDAL' had been done for the wood supply for the chip mill⁵². There are several odd features about this claim. Firstly, the term AMDAL is an Indonesian term for an environmental impact assessment but, under Indonesian law, only new developments require this. So the PT MAL chip mill and port need an AMDAL/EIA, but not the PT HRB feeder concession. Secondly, this document has not been made public to the Indonesia authorities and Jaakko Pöyry only received a summary.

It therefore seems likely that this study of the PT HRB concession was commissioned by UFS in an effort to get approval for its projects from MIGA, the World Bank's insurance agency. MIGA and UFS have been consulting over the last six months and MIGA is reported to have said that it "believed that the project had the potential to be a model of plantation operation in an environmentally sustainable manner."

The provincial authorities only started to adopt a more open attitude after the Indonesian Human Rights Commission (*Komnas HAM*) took the initiative to organise a series of parallel meetings with representatives of the provincial government, investors, local people and local NGOs in 2003.

Komnas HAM's Sub-Commission for Mediation carried out a preparatory meeting on 10 February 2003. This consultation was attended by local officials - including South Kalimantan's governor and the head of the provincial forestry service - members of the regional assembly, academics, company representatives, NGOs and local communities.

Such mediation was much needed because a series of problems over the control and management of South Kalimantan's forests and other natural resources had been reported to *Komnas HAM* since early 2001. Most conflicts revolved around plans to change the zoning of protection forest in the Meratus mountains so the area could be opened up to PT Kodeco Timber's logging, PT Placer Dome's gold mining and paper pulp mills.

⁵² Jaakko Pöyry, 2005 op cit

Along with the threat of forest destruction, there were issues of potential human rights abuses such as the violation of the indigenous peoples' land rights, forest-dependent people's loss of livelihoods and environmental pollution.

The Sub-Commission had sent letters, on behalf of the national human rights commission, asking South Kalimantan's administration, the provincial assembly and the relevant private companies to explain what was going on. This approach did not bring results and was not considered worth pursuing further. Instead, the consultation process was set up to take a closer look at the issues⁵³.

The consultations did not put a stop to plans to build paper pulp and chip mills in South Kalimantan, but they did make the companies take a slightly more open attitude towards the NGOs.

Company representatives said they were prepared to discuss the preparatory process for setting up the mills. However, the information they provided did not match the situation on the ground.

There was no news for about a year until, in February 2004, a local newspaper reported on plans to establish a wood chip mill in the village of Alle-Alle in Kotabaru district⁵⁴.

It turned out that the chip mill company, PT MAL, had been holding public meetings since 2003 in the villages of Tanjung Seloka and Alle-Alle⁵⁵.

These meetings only involved local government officials at sub-district and village levels, and the owners of the land where PT MAL planned to build its factory. The company explained how the mill would be set up. Its public relations staff stated that no dangerous waste would be produced by the chip mill - only sawdust which can be used to generate electricity.

Local people say the company told them that the mill's noise would be just like the general noise level in a village. In other words, there would be no noise pollution. The problems of noisy transport supplying the mill and dusty air caused by the trucks and the sawdust were not even mentioned.

Kotabaru district's state-owned electricity provider (PLN) only supplies electricity to the southern part of Pulau Laut from 6 pm to 6 am. This means people cannot use any electric appliances during the day. So the villagers of Alle-Alle and Tanjung Seloka were naturally delighted that the wood chip mill would mean electricity all day long.

PT MAL also committed itself to providing jobs, especially for those who were prepared to sell their land to the company.

The local authorities created a 'team' to

promote the release of land for the the PT MAL site around November 2004. This represented all levels of local government - district (Kotabaru), sub-district (Pulau Laut Selatan) and village (Alle-Alle and Tanjung) - and the two communities. Its 173 members consisted of all the people who owned the 84,352 ha of land in Alle-Alle and Tanjung Sekola which the company acquired⁵⁶. It was this group which was to negotiate with the company.

In a process of bargaining and (enforced) compromise widely used in Indonesia, the final price agreed between the community members, district government and PT MAL for all land deals was Rp5,500 per square metre (approx US\$0.61). This was 75% less than the price per square metre the landowners initially asked for (Rp20,000/US\$2) and slightly above company's opening offer (Rp3,000/US\$0.3).

According to some community members involved in the team, PT MAL did not want to pay more than Rp5,250/m², while the landowners asked for Rp10,000/m². The head of Kotabaru district, Syahrani Mataja, then proposed that both parties compromised.

The result was not, of course, an acceptable price for the landowners who felt they had lost out. This is significantly lower than current market rates for land in Alle-Alle and Desa Tanjung Seloka. For instance, landowners got Rp40,000/m² when a local clinic was built. Prices may reach Rp100,000/m² if the land is close to the market place or in other commercially attractive areas.

Many landowners were not happy with the deal and only consented because they feared they might lose the opportunity to get some financial benefit from the company's presence in their village. After all, many people were eager to sell their land and PT MAL was not interested in land plots further from the coast for its port development.

Most people in Alle-Alle and Tanjung Seloka welcomed the company's presence, hoping that it would make their villages prosper. The villagers dreamed that roads would be repaired; electricity would be available 24 hours a day; unemployment would fall as people were given jobs by the company; land line and mobile telephone networks would come to the village - and more besides.

Local people also hoped that, with the coming of PT MAL, they could revive the Karya Bersama village cooperative (KUD) in Tanjung Seloka. The cooperative's

⁵³ Komnas HAM Indonesia, 2003

⁵⁴ Radar Banjar, 27 February 2004

⁵⁵ Walhi South Kalimantan, 2005

⁵⁶ Tim Pemilik Lahan Desa Alle-Alle, 2005



A domestic industry in Tanjung Seloka

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activities had dwindled to nothing, but a new management was appointed in December 2004. They saw potential opportunities to do a deal with PT MAL, for instance over the provision of basic food products such as rice, sugar and cooking oil.

A significant number of villagers sold all their land to the company. They sacrificed their fruit trees and coconut palms in the hope that they would eventually benefit from the establishment of the mill in their area and kiss goodbye to poverty. Will their dreams come true?

By late 2005 some 50 families in Tanjung Seloka who owned a total of around 45 ha of land had yet to receive any payment because they were demanding a higher compensation rate of between Rp 15,000/m² and Rp 25,000/m². Their reasons for claiming more money were:

1. Back in November 2004, PT MAL had promised to disburse all payments to the various landowners at the same time. The villagers had requested this to avoid any jealousy, but PT MAL paid out bit by bit. Payments were made without any transparency - people were visited by the company's public relations staff and told to turn up at a certain time in a certain place. This was when the majority of the villagers of Alle-Alle and Desa Tanjung Seloka started to feel wronged. Had PT MAL paid all landowners at the same time, they might not have demanded more money.
2. PT MAL had committed itself to make a 'down payment' of Rp 1 million to each landowner before the end of the Muslim fasting month in November

2004. However, the company only made payments of Rp 750,000 to Rp 1 million and only to around 15 families.

3. Landowners were led to believe that they would receive the full amount of the compensation payments negotiated. In fact, each landowner was charged 'transportation costs' from Tanjung Seloka to Batulicin on the mainland where the payments were made. No-one knows whether these individuals represented the company or the local authorities. The amount charged was Rp 80,000 - twice the usual fare at the time. For the villagers, this made a significant difference.
4. Landowners thought that the company would handle the processing of land certificates (SKT). Instead, they had to do it themselves through the village head, costing each family Rp 200,000-250,000 (US\$20-25).

When one of the team members reported this problem to the head of Kotabaru district, Sjachrani Mataja, he was told to deal with it himself. The villagers were very offended by this remark. As the local government representative, they felt the *bupati* should protect and take care of his constituents' interests. Instead, he chose to ignore the issue.

The latest information from Tanjung Seloka is that the 50 families who demanded more money eventually got nothing. PT MAL decided it only need to use the land it acquired back in 2004⁵⁷.

There are other issues of concern. For example, those who hoped that they would be first in the queue for jobs at the wood chip mill have found out that this is not the case. The signs of conflict among the villagers are starting to show.

Tensions between villagers who feel they have benefited from or lost out in their interactions with the company are a serious potential problem - not only for the communities of Alle-Alle and Tanjung Seloka, but also for the local authorities and the company itself.

As a traditional Indonesian saying goes: fooled by the hope of making a small profit, we sometimes lose something much more valuable (*Kalah mata hilang uang, kalah urusan hilang kerbau*). In the same way, the chip mill development which purported to bring the people of Alle-Alle and Tanjung Seloka prosperity, could cost them dearly through the loss of their livelihoods and conflict in their community.

⁵⁷ Information via telephone from Tanjung Seloka, 19 January 2006

BOX 6

THE PEOPLE WHO PAY THE PRICE

Plans to develop a pulp mill and wood chip mill in South Kalimantan will disadvantage communities living around the mill sites in Satui, Alle-Alle and Tanjung Seloka villages in Kotabaru district.

A field visit by the Banjarmasin-based NGO, LPMA Borneo Selatan, in 2003, found that few people in Sungai Cuka village, Satui sub-district, knew about the plan to build the pulp mill in their village. The villagers' 'involvement' in planning the pulp development was through the village head. A meeting to provide public information about the plan, held on 25 July 2003, was attended by 63 leading community members, representing the village-level administration, Village Council (*BPD*) and religious leaders. The community leaders declared their approval of the Sungai Cuka pulp mill proposal and a list of their names was sent to PT HRB and PT MBBM.

What about the rest of the community? The LPMA field researchers were told that some local people knew nothing at all about plans to set up a pulp plant in their village. The same applies to the wood chip mill development in Alle-Alle village. Information about these plans was only provided to villagers whose land was needed for the mill site.

The rest of the community only heard by word of mouth that a company was developing a project in their village. They didn't really understand either the potential positive or negative impacts. The company had not involved them in the planning for the Alle-Alle chip mill because these villagers were of no direct concern. However, the whole community will suffer the impacts of this company's operations, especially those living closest to the mill.

The majority of Sungai Cuka villagers belong to the Banjar ethnic group. Fishing is their main source of livelihood, in addition to growing rice and other crops. Their way of life is the same as the Alle-Alle and Tanjung Seloka villagers, the majority of whom are ethnic Mandar and Bugis.

The forests, rivers, sea and beaches are their lifeblood. If these resources are destroyed by the pulp and woodchip industry, where will they go? They have no experience of employment as mill workers (i.e. labourers), and they would need time to adjust. Despite this, the company claims that the mill will be a new source of income for the community.

Does the company want to give technical training to villagers who are used to casting fishing nets so that they can operate modern machinery they had never previously seen? If not, where is this new source of income for the community?

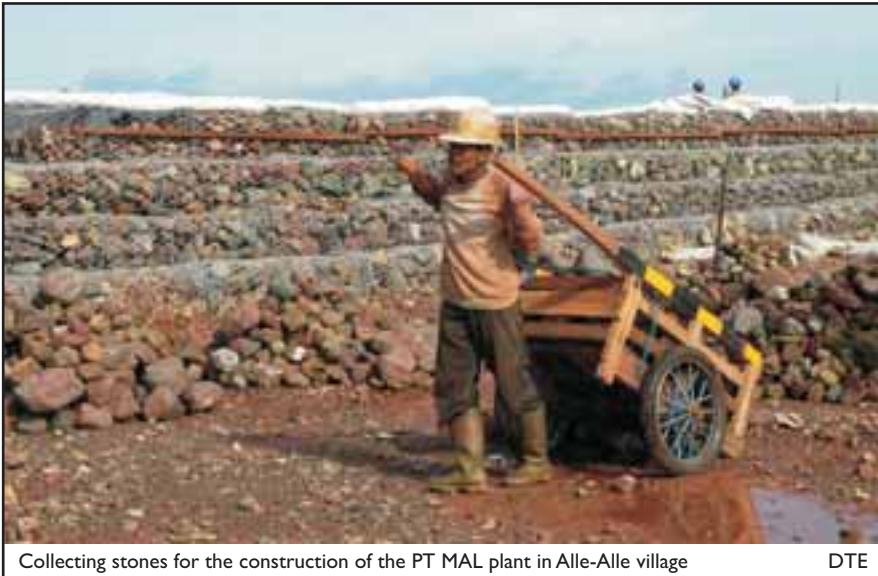
In its public information campaign, UFS has said the chip and pulp mill projects would be environmentally friendly and would not constitute a threat to local people's livelihoods in the future. In reality, the company did not provide enough information about their plan to dispose of waste into the sea and the impacts of this. Marine pollution is bound to threaten the fisheries on which the villagers depend.

Sources:

- LPMA Borneo Selatan, 2003

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THE CHIP MILL PORT



Collecting stones for the construction of the PT MAL plant in Alle-Alle village

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timber a year. The total legal quota for timber felled from natural forests in 2005 was only 5.6 million m³ for the whole of Indonesia⁵⁹. This is equivalent to 220,000 ha of acacia plantation per year (see Table 5). UFS does not have access to that much timber from PT HRB and the few other existing plantation companies already have customers - such as Kiani Kertas or pulp mills on Sumatra.

When PT MAL staff told local people about the project, they did not talk about the negative impacts that the construction of the

In addition to the chip mill, the company also intends to build a port at Tanjung Setigi in Alle-Alle.

PT MAL applied for a permit to build this in a letter to the Indonesian Ministry of Transportation on 5 January 2005⁵⁸. At the time of writing this report, PT MAL had not yet received the permit.

Timber from South and East Kalimantan will be delivered to the integrated port-mill complex on Pulau Laut where it will be processed into wood chips. These will then be shipped out to supply the paper industry. But although the chip mill is quite close to the site on the mainland where UFS intends to build its pulp mill, this does not mean that is where the wood chips will go. Firstly, most Indonesian pulp mills have their own chipping units to turn raw logs into small pieces which are easier to process into pulp. Secondly, UFS has signed an agreement with CMEC to buy 90% of the chip mill production and have an option on the other 10%, so all the production from Alle-Alle will probably go to China. It does not make economic sense for PT Kiani Kertas or (when built) the Satui pulp plant to buy in these wood chips at the full market price they can find cheaper sources.

It is not known how long this agreement is intended to last but, while it does, the PT MAL chip mill is in effect a means of stripping Kalimantan's forests for export. The chip mill consumes over 3 million m³ of

port and the chip mill's operations would have on their lives. However, the port's environmental management plan (RKL) lists the following six topics as areas of potential concern⁶⁰:

1. Water quality

The level of Total Suspended Solids (TSS) and turbidity are expected to increase significantly due to the digging and land clearance taking place during construction.

Increased TSS levels and turbidity could occur in the harbour area due to ships stirring up the seabed and to run-off from the wood chip piles.

2. Aquatic life

A reduction in water quality will lead to a decline in the numbers and diversity of marine life in the area close to the port.

A general deterioration of public health may lead to a higher incidence of environmentally-transmitted diseases. Changes in sanitation due to land clearance and increased population could increase the incidence of water-borne illnesses such as diarrhoea, dysentery and malaria.

⁵⁸ No.025/MAP/1/2005, PT MAL, May 2005

⁵⁹ SK Direktur Jenderal Bina Produksi Kehutanan, Oktober 2004

⁶⁰ PT MAL, op cit

3. Air pollution.
Greatly increased levels of dust are anticipated, in excess of permitted levels, which will adversely affect living conditions in the area.
4. Soil
Soil quality is expected to decrease due to leaching and soil compaction caused by land clearance and other construction activities.
5. Hydrology
Increased surface run-off is expected to cause higher levels of erosion and sedimentation during construction works.
6. Hydro-oceanography
The movement of ships in and out of the port may generate waves that cause coastal abrasion.

These six factors will have serious impacts on the sustainability of local livelihoods. The majority of the villagers belong to the Mandar and Bugis ethnic groups who make their living from fishing.

With only 30% of the port construction completed, the inhabitants of Alle-Alle are already starting to worry. The rocks used for building the port are being taken from the shore and this has already caused significant changes to the depth and clarity of the water along the beach at Alle-Alle.

Despite an official warning from the Kotabaru district fisheries service, the company continues to take rocks from the shore to use them as building material for their port. Local villagers collect the rocks and then sell them to PT MAL's building contractor, PT WIKA, at Rp67,000/m³. They can make more money doing this than as day labourers who the company only pays Rp27,500 per day (US\$2.75).

Those community members not engaged in the building of the factory are concerned about the changes to their environment. For them, the beach and the sea are the basis of their livelihoods - the men go out to fish and the women collect shellfish on the beach in the mornings and afternoons.



Construction of the port for the Alle-Alle wood chip mill

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PT KIANI KERTAS TAKEOVER PLANS



The Kiani Kertas pulp factory

www.kiani.com

While the start-up date of the Satui pulp project remained uncertain, UFS unexpectedly announced its intention to take over PT Kiani Kertas (KK) in East Kalimantan⁶¹.

This emerged after UFS successfully took over PT Succsani Smart Work (SSW) on 27 July 2005. Two

days before, UFS signed a joint operational management agreement with SSW⁶². Nothing is known about PT Succsani's background, track record or previous relationship with PT KK. Under this deal, PT SSW manages the factory's operations and receives proceeds from the pulp sales.

The mill resumed production with its first batch of pulp appearing in late September 2005⁶³. Production had ground to a halt in May that year when the company was, in effect, bankrupt⁶⁴.

A number of Kiani subsidiary companies - part of Bob Hasan's former forestry empire - were sold as part of this transaction: PT Kiani Lestari, PT Wenang Sakti,

⁶¹ UFS, press release 27 July 2005

⁶² Kompas, 16 August 2005,

⁶³ UFS press release, 28 September 2005

⁶⁴ Straits Times, 17 October 2005

BOX 7

KIANI KERTAS

PT Kiani Kertas (KK) is a paper pulp company set up by timber tycoon Muhammad 'Bob' Hasan, a close friend of former president Soeharto, in 1990. It owns a 525,000 tonne paper pulp plant at Mangkajang in Berau District, East Kalimantan. Construction began in 1994 with first production in 1997.

Prabowo Subianto, former commander of the notorious Indonesian Special Forces (*Kopassus*) and Soeharto's son-in-law, now acts as president director of Kiani Kertas.

The pulp plant, located far from any major towns, has its own air strip, deep water harbour, water and waste treatment plants and a town site which can accommodate 800 workers. The site covers 3,400 ha.

Even before Prabowo's company took over PT KK, there were reports of land rights violations,

inadequate compensation, intimidation of plaintiffs and environmental pollution. Security around the plant is said to be tight due to close links between PT KK and the military.

Until 2001, Kiani Kertas' main supplier of timber was the PT Tanjung Redeb Hutani HTI concession, also part of Hasan's group. Later suppliers included PT Sumalindo Lestari Jaya, PT Karya Lestari and the state-owned enterprise PT Inhutani. The company was also reported to be importing timber as wood chips from Australia, but timber from illegal logging was a more likely source.

Sources:

- Watch!Indonesia, August 2005
- Straits Times, 17 October 2005

PT Alas Helau, PT Kiani Hutani, PT Belantara, PT Tusam Hutani, and PT Gunung Gajah. The timber concession HTI PT Tanjung Redeb was not included in the deal⁶⁵.

UFS' (then) Chief Executive Officer, Kishore Dass, explained that taking over Kiani Kertas was in line with the company's strategic vision to become the world's leading paper pulp producer, in a written announcement published by the major Indonesian daily newspaper Kompas⁶⁶.

Part of this plan is a cooperation agreement signed by UFS and PT Inhutani II for the state-owned forestry company to supply 1 million tonnes of *A. mangium* timber by 31 December 2008⁶⁷. This will be used as raw material for PT Kiani Kertas' pulp mill in East Kalimantan.

UFS' vision to become one of the world's most important paper pulp producers may soon be one step nearer⁶⁸.

At the time of writing, UFS/Kingsclere were close to buying PT KK from PT Fayola and PT Langass. It is not entirely clear how these offshore companies got involved. PT Fayola Investment (registered in Mauritius) is controlled by Prabowo (see Box 7). Langass (British Virgin Islands) took over US\$230 million of Kiani Kertas debts (equivalent to about 30% of PT KK shares) in January 2006. Langass' owners are not known⁶⁹.

Kingsclere is an Indonesian investment company owned by Wisanggeni Lauw who holds around 15% of UFS' shares. Wisanggeni was reported to be a

⁶⁵ Bisnis Indonesia, 14 February 2006

⁶⁶ Kompas, op cit

⁶⁷ Sinar Harapan, 8 August 2005

⁶⁸ UFS, Annual Report 2005

⁶⁹ Ardi Y, 25 January 2006

Table 6: UFS Projects in Kalimantan

Major companies still involved with UFS' projects

Name	Nationality	Amount of Investment	Type of Investment
China National Machinery & Equipment Import & Export Corporation (CMEC)	China	- US\$690 million	- Construction of PT MBBM paper pulp plant at Satui
		- US\$18 million	- Construction of PT MAL chip plant at Alle-Alle village
Andritz AG	Austria	- US\$250 million	Pulp mill and chip mill equipment
Raiffeissen Zentralbank Österreich AG (RZB-Austria)	Singapore	- US\$21 million	Construction of PT MAL chip plant
China Export & Credit Insurance Corporation (Sinosure)	China		Insurance cover for proposed Satui pulp plant
CellMark	Sweden		Purchase of paper pulp production from Satui plant for first 10 years
Merrill Lynch	USA		Financial adviser in PT Kiani Kertas takeover
Vivendi Water	France		Supplier of water treatment plant
Cornell Capital Partners	USA	- US\$165 million	Equity line of credit

Sumber:

- UFS, 2004
- UFS, 2005
- UFS, 28 April 2005
- UFS website, www.ufs.com.sg
- Bisnis Indonesia, 14 February 2006
- DTE Newsletter 62, August 2004
- Smart Investor, September 2005

former employee of Probosutedjo and nephew of timber baron, Prayogo Pangestu⁷⁰.

The two major creditors of PT Kiani Kertas - Indonesia's Bank Mandiri and US investment bank JP Morgan - have failed to agree deals with potential purchasers during the past year⁷¹. Bank Mandiri is insisting that PT KK's new investors should pay an outstanding debt of US\$ 201 million plus accumulated interest of US\$ 12 million⁷². These debts have their roots in loans taken by PT KK before the 1997 Asian monetary crisis.

Bank Mandiri attempted to negotiate a deal with the Widjaya family that controls the massively indebted Riau pulp giant, APP, and its parent group Sinar Mas. However, Prabowo refused to sell and even invited APP's rivals, RGM - another company notorious for its bad debts and poor environmental record - to open negotiations over PT Kiani Kertas. So far, these have not materialised⁷³.

A deal proposed between JP Morgan, PT KK's largest foreign creditor, and Kingsclere (UFS/Lauw) broke down in August 2005⁷⁴. PT KK owes the American bank at least US\$70 million.

UFS and JP Morgan then started to negotiate separately with Lauw for PT KK. UFS took on Deutsche Bank to advise it on the deal and, presumably, to help raise finance. At the same time, JP Morgan tried to combine forces with PT Sampoerna Strategic (part of the giant Indonesian clove cigarette company) in a rival bid for the pulp company. However, this deal foundered in January 2006⁷⁵.

After PT Sampoerna dropped out, UFS was well positioned to take over PT KK. The fact that Deutsche Bank has withdrawn its support to this plan is

not a major problem. Merrill Lynch, a well known American financial management and advisory company, has done the due diligence study⁷⁶ and New Zealand banker ANZ has stepped into Deutsche Bank's shoes as UFS' financial adviser⁷⁷.

Why is UFS so interested in PT KK? The reasons are fairly simple: apart from making huge profits, this would allow UFS to establish itself as one of Indonesia's top four paper pulp producers⁷⁸.

The price for paper pulp on the world market is US\$500 per tonne, while production costs amount to about US\$350/t. This generates a gross profit of US\$150 for every tonne of paper pulp. As PT KK can produce up to 525,000 tonnes of paper pulp per year, this translates into annual gross profits of US\$78.75 million⁷⁹.

Taking over PT KK not only gives UFS a working pulp mill, but also paves the way to enter markets in China, as APRIL and Asia Pulp and Paper (APP) have done. Low transportation costs to other countries in Asia, such as Japan, Korea and India, are another factor⁸⁰.

⁷⁰ FT.com, 3 Nov 2005

⁷¹ Kompas, 9 January 2006

⁷² Kompas, 12 December 2005

⁷³ Ardi Y, 15 November 2005

⁷⁴ paperloop.com, 26 August 2006

⁷⁵ Kompas 19 January 2000

⁷⁶ Bisnis Indonesia, 14 February 2006

⁷⁷ International Financing Review, CIFOR, 13 May 2006

⁷⁸ FT.com 4 July 2005

⁷⁹ Straits Times, 17 Oct 2005

⁸⁰ UFS Ltd., 20 February 2006

PT KIANI KERTAS' BAD DEBTS

PT Kiani Kertas cost around US\$1.3bn to set up. Around US\$670,000 was financed by overseas loans while US\$450,000 came from domestic loans.

The pulp mill company received a Rp250 million loan (then US\$100 million) from the Indonesian government's Reforestation Fund in 1996, thanks to Presidential Decree No. 93. Interest rates on this loan were 4% below bank rates. In addition, Soeharto gave six companies a tax holiday in mid-1997: Kiani Kertas got a 10-year tax break.

On top of that, a syndicate of 24 foreign creditors headed by Japan's Sumitomo Bank provided PT KK with a credit facility of US\$120 million in March 1997 to expand production.

Within two years of all this money being thrown at it, PT KK was in deep trouble. After Indonesia's 1997-8 financial crash, Bob Hasan's empire of banking, real estate and forestry companies collapsed under huge debts. Many loans had been secured by the Bank Umum Nasional, owned by Bob Hasan, and banks owned by other members of Soeharto's elite which went bankrupt. Hasan personally owed over Rp5 trillion (US\$500,000 million).

Some of his heavily indebted forestry companies were taken under the wing of the Indonesian Bank Reconstruction Agency (IBRA/BPPN), including around US\$400 million of Kiani Kertas' outstanding domestic debts.

PT KK got further government help in the form of a debt restructuring deal by IBRA. US\$226.5 million of the 'sustainable' debt was restructured into a 10-year loan, including a two-year grace period and annual interest of around 12%. Another US\$246.6 million was converted to mandatory convertible bonds. IBRA claimed this rescue package would result in the repayment of 47.7% of PT KK's total state debts.

Eventually, the Indonesian state-owned Bank Mandiri took over US\$201.24 million of PT KK's convertible debts from the Bank Restructuring

Agency on 15 November 2002. A further Rp7.1 trillion (then US\$500 million) was taken over by PT Energy Nusantara via another enterprise, PT Anugra Cipta Investa (ACI). Nusantara Energy is owned by Prabowo Subianto (79%), Widjono Hardjanto (1%) and Djohan Teguh (20%) in a deal that has recently been the subject of a corruption case.

Unfortunately, Bank Mandiri's acquisition of PT KK's debt did not solve the pulp company's problems. No loan repayments have been made since November 2003 and Bank Mandiri must set aside Rp1.8 trillion (US\$180 million) in its annual accounts to cover this debt.

Bank Mandiri is keen for any kind of deal to relieve the burden of PT KK's debt, as the national Bank Indonesia cannot extend credit limits indefinitely. Bank Mandiri wants to reduce its non-performing loans by 5% in 2007 and that means tackling 30 heavily indebted clients, including PT KK.

Kiani Kertas is also thought to owe \$120-200 million to international lenders including Japan's Sumitomo and US investors Lehman Brothers, JP Morgan and Amroc. By 2006, Kiani Kertas' total debt was around US\$ 867 million.

Sources:

- TAPOL Bulletin No. 143, October 1997
- Media Transparansi Online, October 1998
- Human Rights Watch, 2003
- Bisnis Indonesia, 24 November 2005
- Financial Times, 23 May 2005
- Koran Tempo, 4 April 2005
- Gatra.com, 5 June 2005
- Insinyur Kimia Online, 16 August 2005
- Bisnis Indonesia, 22 August 2005
- Bisnis Indonesia, 15 September 2005
- Riau Post, 22 December 2005
- Kapan Lagi.com, 13 January 2006
- International Financing Review, CIFOR, 13 May 2006
- Bambang Setiono, Financial Institutions and Forest Crimes, <http://www.infid.be/Forestry.pdf> 2001
- Down to Earth Newsletter 48, February 2001
<http://www.dprin.go.id/ENG/Publication/IndReview/2004/20040621.htm>

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INTERNATIONAL ACTION



Protest outside Deutsche Bank, German

Robin Wood

Indonesian national and local NGOs have worked with international NGOs to lobby against international backing for the South Kalimantan pulp and chip plants on the grounds that these projects damage the environment and local peoples' livelihoods.

Down to Earth circulated information in early 2001 about plans to build a pulp plant in South Kalimantan, shortly after the governor's announcement that an international consortium would back the project. Activists from Germany, Finland and Sweden have all helped raise concern at the international level through reports and films produced in co-operation with Indonesian groups.

Indonesian and international NGOs belonging to the network ECA Watch investigated which export credit agencies might give financial support to the pulp plant and lobbied against their involvement. A letter, signed by 65 NGOs from 19 countries, was sent to the World Bank-agency MIGA (Multilateral Investment Guarantee Agency) in 2003 by US-based Environmental Defense to persuade it against the project. UFS withdrew their application from MIGA, but may be considering a new application. NGOs are also briefing the Austrian export credit agency, OeKB.

In 2003, environmental campaigners led by Milieudefensie (Friends of the Earth Netherlands) secured the withdrawal from the pulp project of Netherlands-based Akzo Nobel⁸². The company had signed up to build a plant to produce bleaching agents for the plant, through its chemicals subsidiary, EKA. Its investment represented around 8% of the total pulp investment cost. However, in recent months, EKA has

indicated that it is still interested if conditions are met on the sustainable supply of raw materials. Dutch NGOs have also met with UFS' representatives to discuss their concerns.

By early 2005, it became clear that UFS was planning a wood chip mill as well as a pulp mill in South Kalimantan. The international forest research centre, CIFOR, produced reports in 2004 and 2005 which raised questions about the new pulp and chip mills in the context of Indonesian government commitments to international creditor nations about down-sizing wood processing industries⁸³.

As two Austrian companies were heavily committed to the UFS pulp and chip mills (the major bank Raiffeisen Zentralbank Österreich and engineering company Andritz AG), Austrian environmentalists - led by Global 2000 (FoE Austria) - took action against both companies⁸⁴.

In August 2005, twelve activists blocked the gates of an Andritz factory in Graz for a whole day, attracting much media attention⁸⁵. Global 2000 and the US NGO Environmental Defense launched a letter writing campaign to Andritz and RZB in November

⁸¹ Kompas, 22 November 2000

⁸² Milieudefensie, 2002, www.milieudefensie.nl

⁸³ Jurgens et al, CIFOR 2005

⁸⁴ DTE newsletter 68:18-9

⁸⁵ Global 2000 website <http://www.global2000.at/index3.htm>.



Austrian NGO protesting against Andritz'

Global 2000

2005⁸⁶ (see Appendix 4). RZB met environmental campaigners, but claims that it is now too late for it to pull out of the deal with UFS.

The German campaigning NGOs, Robin Wood, Rettet den Regenwald, Watch!Indonesia and Urgewald worked closely together to put pressure on Deutsche Bank to review its planned loans to help UFS procure Kiani Kertas. Letters requesting a meeting to discuss the issue were backed with demonstrations outside Deutsche Bank's main office in Germany⁸⁷. Deutsche Bank announced in January 2006 that it "no longer holds a mandate with UFS"⁸⁸. American NGOs will be watching Merrill Lynch, which has done the due diligence study for the UFS Kiani Kertas deal, and the financing company, Cornell.

UFS and its international financiers are now taking Indonesian and international NGOs seriously. Their consultants have organised a series of meetings in Europe and Indonesia in recent months. It remains to be seen whether these will result in any changes which will genuinely benefit local communities and their environments.

⁸⁶ <http://forests.org/action/alert.asp?id=indonesia>

⁸⁷ See Robin Wood website: <http://www.umwelt.org/robin-wood/german/presse/051209.htm>

⁸⁸ Robin Wood, Dec 2005, pers com

BOX 9

BANKING ON PAPER

The International Finance Corporation (IFC), the World Bank Group's private sector lending agency, is also linked to UFS' efforts to gain international credibility for its pulp plants and wood chip mill. The state-owned forestry company, Inhutani II, has a 50,000 ha acacia plantation on Pulau Laut - a likely source of raw material for the Alle-Alle chip mill and the Kiani Kertas pulp mill. Inhutani II has signed a 3-year supply contract with UFS for a total of 1 million m³ of timber.

In May 2006, this became the first acacia plantation to gain membership of WWF's Global Forest and Trade Network (Nusa Hijau in Indonesia) - a scheme intended to promote 'eco-friendly' timber to international buyers. Members must show a commitment to achieving Forest Stewardship Council (FSC) sustainable forestry certification within 5 years. Inhutani II was assisted by the IFC's Program for Eastern Indonesia SME Assistance (IFC-PENSA).

IFC is playing an increasingly important role in financing pulp and plantation projects in the South, most recently in two huge controversial pulp plants in Uruguay.

International banks have shown little accountability to date in the financial service they provide to Indonesia's pulp sector. The Equator Principles - which commit banks that sign up to funding only environmentally and socially responsible development - do not apply to the

commercial bank loans or bond and share schemes most often used to finance plantation or paper pulp ventures. So JP Morgan, Deutsche Bank, Merrill Lynch, Cornell Capital and other investment banks do not feel bound to stick to this voluntary code in their dealings with UFS.

The Equator Principles, in effect, commit members to screening all projects against the IFC's Safeguard Policies. But these do not provide communities with the protection they promise. The IFC, like other members of the World Bank Group, has a development mandate. However, the IFC's priorities are acting as a partner to industry rather than promoting poverty reduction. Also, it has weakened its social and environmental controls.

The IFC usually works in a reciprocal relationship with another World Bank arm - MIGA. After IFC has facilitated financing for a company, it opens the door for MIGA to insure the company against political risk - including social conflict. Alternatively, MIGA's risk protection can help a company attract funding via the IFC.

Sources:

- IFC press release, 11 May 2006
- FoE International mailing, 13 April 2006
- CIFOR staff, May 2006, pers com
- Environmental Defense press release, 21 February 2006
- Milieudefensie, March 2006
- BankTrack website, 28 April 2006

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CONCLUSIONS



Fisherfolk's house in Alle-Alle

DTE

Alle-Alle, Sungai Cuka and Mangkajang are ordinary Indonesian villages in the process of becoming part of an international industrial venture. The social and environmental issues which their communities face are not isolated local issues, but an integral part of the global market for paper pulp and international finance. Companies based in USA, Europe, Scandinavia, China, Singapore as well as Indonesia are involved in these cases.

There is a close financial connection between UFS' developments of the PT MAL chip mill and PT MBBM and PT Kiani Kertas pulp mills. UFS' pulpwood plantation (PT HRB) is also central to their success. In mid 2005, UFS shares tumbled due to trader gossip that the company was just 'concept stock' - a venture claiming to have assets with which it can do nothing⁸⁹. The profits from the chip mill and pulp production from Kiani Kertas will increase UFS' credibility and make it easier to leverage other loans. Experience with APP and APRIL in Riau, Sumatra, is that large loans are then used to justify expansion of mill capacity on the grounds that economies of scale speed up repayment.

The revenues from PT MAL and PT KK will also allow UFS to put more money into developing the PT HRB plantation and Satui pulp mill. UFS could generate more cash by clearing some or all of the natural forest within the areas it has acquired. The 73,000 ha of forest represents some 4 million m³ of commercially valuable timber⁹⁰ worth over US\$500 million on the international market.

There is much uncertainty over the source of the timber which UFS will use as the raw material for its three ambitious ventures. However, there are several

clear conclusions about the PT MAL wood chip mill and the plantations and pulp mills on which it depends.

Firstly, events are likely to move fast. UFS' chip mill is under construction and the company has made it clear that work on the Satui pulp mill will start as soon as the PT KK deal goes through. Any involvement by IFC and MIGA will boost UFS' financial standing. Forestry minister Kaban has a strong background in economics and started his ministry with a call to make the forestry sector generate more revenues for the Indonesian economy, as it did in the 'good old days' of 'Bob Hasan'. His priorities are increasing Indonesia's exports, rather than reducing overcapacity in its unsustainable wood processing industry. So, with wood chips fetching US\$120-130/tonne or more on the international market, there is much potential revenue for UFS/PT MAL and local and central government.

Secondly, there are some very powerful stakeholders involved. At the national level, the dominant player in the Kiani Kertas deal is Prabowo, now a highly successful businessman due to his connections with the Soeharto family but formerly a Lieutenant General in the Indonesian military - one of the same intake as Indonesia's President Bambang Susilo Yudhoyono.

At the international level there is China's burgeoning paper market where, in order to meet domestic demand, growth in pulp mills is running far ahead of setting up plantations to supply them. China prefers to buy in logs, chips or pulp and convert them into paper and other wood products to increase employment at home.

It is not surprising that CMEC is providing the technical expertise and finance for constructing the chip mill plant in return for first option on the purchasing the majority of its output. UFS' larger Indonesian rivals in the pulp business already have their foot in the door in China - APRIL has a supply contract with Finland's UPM-Kymmene in Changshu and APP owns several plantations and pulp plants, mainly in Yunnan province⁹¹.

The final conclusion is that communities in South Kalimantan are missing out on the opportunities for local democracy presented by the fall of Soeharto and the introduction of regional autonomy. The people of Alle-Alle and Sungai Cuka are caught between UFS'

⁸⁹ zaobao.com, 25 August 2005

⁹⁰ RePPPProT, 1990

⁹¹ see DTE 52, February 2002

ambitions to be one of the top four pulp companies in Indonesia and a government which is proud of being the cheapest paper pulp producer in the world. Participation in local decision-making is being sacrificed to the profit motive. Although Indonesia has a new elected president, the pattern of ruthless exploitation of natural resources continues - now driven by local elites as much as Jakarta. Meanwhile there is a lack of investment in the sustainable use of resources.

The information provided in the previous section shows that the establishment of an integrated chip mill by UFS in Alle-Alle village on Pulau Laut, South Kalimantan, is completely unacceptable on social and environmental grounds. The Satui pulp mill will also be ecologically and financially unsustainable. The main reasons for this conclusion are:

Lack of information and transparency:

- Local communities, government officials and policy makers have not received the detailed information they needed to base decisions on before the chip mill project started. They had no access to independent sources about the potential benefits and risks of this project to people's livelihoods and environment.
- The majority of the people were not consulted. They have received only scraps of information passed from person to person. There were no meetings where whole communities were invited.
- The process of producing and approving the Environmental Impact Assessment (AMDAL) was not open and participatory for the chip and pulp mills. Local CSOs only have limited access to the final reports.
- Only a few individuals in higher positions within the communities, company and local government actually understand the technical implications of the chip mill or pulp mill projects. Nevertheless, the provincial and district authorities have supported the development of the paper pulp and chip industry from the very beginning.
- There has been a lack of transparency about the relationship between the three companies that UFS is seeking to develop.
- The complex deals over shares and debt between holding companies within holding companies in UFS conceal the identities of the people in power. Meanwhile, the communities are left to deal with public relations staff and contractors who have little information and no authority to take decisions.

- The source of the timber for the chip mill and pulp mills is far from clear because UFS has not presented convincing data.
- UFS has been coy about the important agreement with CMEC to purchase 90% of the chip mill's production (with an option on the remaining 10%). No details were given to UFS' shareholders and the public in the one small mention in its Annual Report and there was no announcement in the Singapore Stock Exchange.
- Although the law suit between UFS and Indonesia's Forestry Department ended with the Supreme Court verdict in UFS's favour, there is still a problem between them: the issue of the legality of timber from its HTI concession. This will only be resolved when the minister of forestry issues a new HTI licence in HRB's name.
- UFS has not been transparent about the taxes, royalties and other payments to local and central government which it has made or will make for the chip mill or the future pulp mill in South Kalimantan.

Negative social impacts:

- UFS' companies and the local authorities have withheld information and not honestly answered local people's questions about the chip mill, so they are ill-prepared for any negative impacts on their livelihoods.
- The unfair, secretive way of handling land compensation payments has generated a lack of trust within the community and sown the seeds of social conflict.
- UFS/ PT MAL has raised high expectations among the local communities on Pulau Laut. However, chip mills are mechanised processes which provide little local employment. Most of the work is for unskilled labour, such as loading and unloading timber and wood chips and cleaning up sawdust.
- People in Alle-Alle and Tanjung Seloka who sold all their land for relatively low rates of compensation have either become landless or had to purchase land far from their village. This is likely to change land use and employment patterns and community life.
- UFS and the local authorities have also misled communities in the Satui area about local employment prospects in the paper pulp mill. The first press reports talked of tens of thousands of jobs⁹². But, like chip mills, pulp mills are highly

⁹² Banjarmasin Post, 20 December 2000

mechanised and employ, at most a few hundred people. Low education levels among local communities mean most will be on low paid daily rates, while skilled outsiders become permanent staff.

- The chip mill and pulp mill and integrated ports will bring huge social changes to both areas. Bars, owned by South Kalimantan's business elite will spring up to supply workers from other areas, making alcohol more available and prostitution more likely. The incidence of HIV/AIDs is much higher in ports than elsewhere in Indonesia.



Children usually walk to school in Alle-Alle

DTE

Growing environmental costs:

- The combined effect of Indonesia's prolonged economic slump, the introduction of regional autonomy and lack of funding incentives from central government has been that most timber plantation concessions in South Kalimantan only clear natural forest in their concessions or harvest existing plantations - they have stopped replanting. So the capacity of HTI concessions in South Kalimantan to provide sustainable supplies to forestry based industries has is low and will remain so for the next decade.
- The capacity of UFS' chip mill far exceeds current production from its plantation. The majority of this production will be sold to CMEC, probably for export to China. Yet the same plantation is also to be used for the PT MBBM pulp mill planned at Sungai Cuka. If the Kiani Kertas deal goes through, it will also need sustainable sources of timber if UFS is to meet its pledge.
- The fact that UFS's chip mill does not have reliable sources of raw material from plantations poses a serious threat to the natural forests in South Kalimantan.
- South Kalimantan's forests in the Meratus mountain range and on Mount Sebatung are already severely degraded due to illegal logging. Floods and land slides have become a yearly recurring phenomenon caused by reduced water absorption capacity. The new chip mill potentially creates additional pressure on local forests and increases the risk of natural disasters during the rainy season.
- Legal, but destructive logging is as much of an issue in forest destruction as illegal logging. Some 40,000 ha

of natural lowland forests on Pulau Laut are likely to be clear felled and replaced by pulpwood plantations. More than 70,000 ha of forest remaining in PT HRB's plantation is currently listed as 'assets' worth S\$150 million (US\$94 million) in UFS' annual audited accounts⁹³.

- Acacia plantations do not fulfil the same ecological, cultural and social functions as tropical rainforest. Forest destruction destroys biodiversity. South Kalimantan's forests are home to several endemic species of flora and fauna, including the proboscis monkey.
- The removal of rocks as ballast for construction of the chip mill port has made the formerly crystal clear water off the coast around Alle-Alle turn murky brown. The coming and going of ships will have a detrimental effect on the local fisheries, causing serious long-term impacts for men and women who currently live by fishing. The loss of livelihoods will increase poverty. Fewer fish means a poorer diet for local communities.
- The EIA for the PT MBBM pulp plant shows that large-scale water pollution is anticipated in Satui. This will cause a loss of livelihood and poorer health for the local community which depends heavily on fishing. People in the area have not been informed about this potential negative impact on their lives.

⁹³ UFS, Annual Reports 2005, p64



Alle-Alle residents

DTE

Indonesia has one of the world's highest deforestation rates. The paper pulp industry is the major consumer of timber from plantations and natural forests in Indonesia. The Indonesian government has made public commitments, nationally and internationally, to restructure the country's wood processing industry.

There should therefore be no expansion of Indonesia's pulp industry. No new chip mills or pulp mills should be built, or existing mills allowed to increase their capacity, unless and until there are sustainable supplies of raw materials which do not damage local communities and their environments, including forests. Moreover, Indonesia does not need any more large-scale monocultures of exotic tree species. Plantation development must respect indigenous peoples' rights and enhance economic, ecological and social stability. For these reasons,

The Indonesian government should:

- Refuse to issue a permit to UFS or any other company in South Kalimantan to develop wood pulp or chip plants until the supplies of raw material have been clearly identified and full information has

been provided about the potential positive and negative consequences of these factories;

- Commission an independent investigation into the proposed sources of timber for the chip mill in Alle-Alle;
- Stop the renewed production of pulp by Kiani Kertas until an independent review has reported on the sustainability of its timber supply;
- Give local communities opportunities to participate in the development of their area, by providing access to information about plans for local forests, their exploitation and other forestry related information;
- Support community-based forest management initiatives which are sustainable both from an environmental and a livelihoods perspective;
- Adopt development policies which promote sustainable natural resource use and which recognise indigenous peoples' rights;
- Foster local communities' interests rather than prioritising the interests of investors that are potentially damaging to people's livelihoods and environments;
- Require all paper pulp plants in Indonesia to prove that their sources of timber are legal and sustainable.

International investors should:

- Refuse to invest in projects that have the potential to cause serious environmental and social damage, do not respect local communities' rights and have not been agreed without securing the free, prior and informed consent of indigenous communities;
- Pay full compensation to local communities for any damage caused to their environment or livelihoods;
- Withdraw financial and political support from companies and their contractors who damage local people's livelihoods or environments and/or violate their rights;
- Fulfil their obligations as stipulated by international law and adopt sustainable development practices in accordance with the Equator Principles.

Governments of investors' home countries should:

- Provide financial and political support to policies,

legal reforms and programmes at local or national level in Indonesia that promote sustainable community-based natural resources management;

- Support and promote international legislation on corporate accountability so that companies adopt the same standards in Indonesia and other countries where they operate.

UFS should:

- Provide full, accurate information to Indonesian communities, particularly in those in South Kalimantan, about its plans for the wood pulp and chip mills, including their potential positive and negative aspects;
- Adopt measures to minimise the social and environmental impact of its chip mill and port in Alle-Alle on the local community;
- Ensure that no timber processed in the Alle-Alle chip mill comes from illegal or environmentally destructive sources;

- Focus on procuring sustainable timber supplies for Kiani Kertas from the group's HTI concessions (PT HRB), respect the rights of local communities and protect remaining forest in the area;
- Cancel its plan to set up the Satui paper pulp mill because the PT HRB plantation does not have the capacity to supply pulp wood to Kiani Kertas as well as a paper pulp mill in Satui;
- Manage the planted area of PT HRB's concession effectively to maximise production;
- Protect all remaining natural forest areas within PT HRB's concession area;
- Protect and manage sustainably all remaining natural forest areas on Pulau Laut (Kotabaru district);
- Plan with local communities how to reforest PT HRB's concession, and manage remaining forest within it, in ways that respect the rights of the local communities and promote ecological, economic and social stability.



The next generation in Alle-Alle

DTE

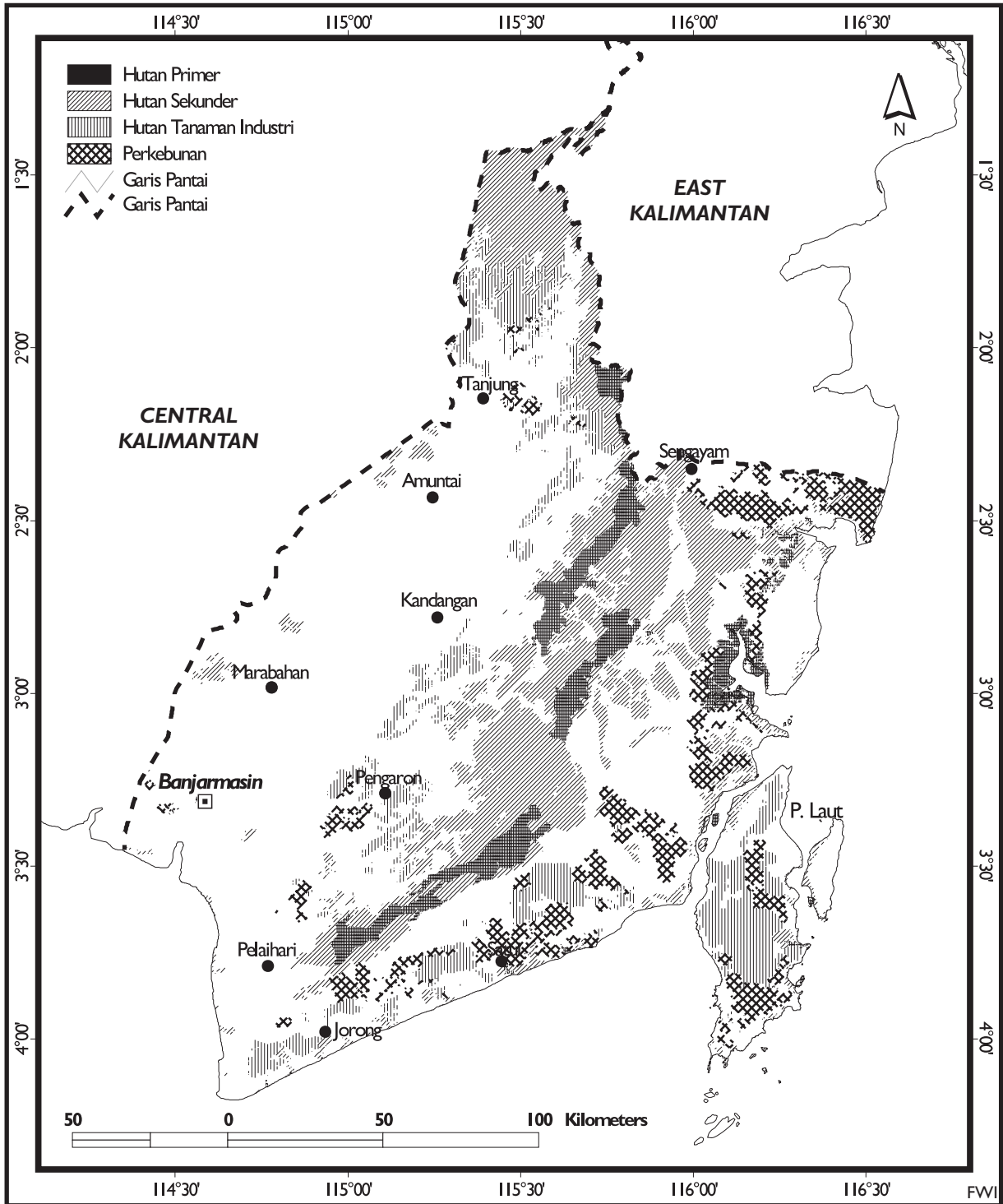
APPENDICES

APPENDIX I: UFS'S COMPANIES STRUCTURE

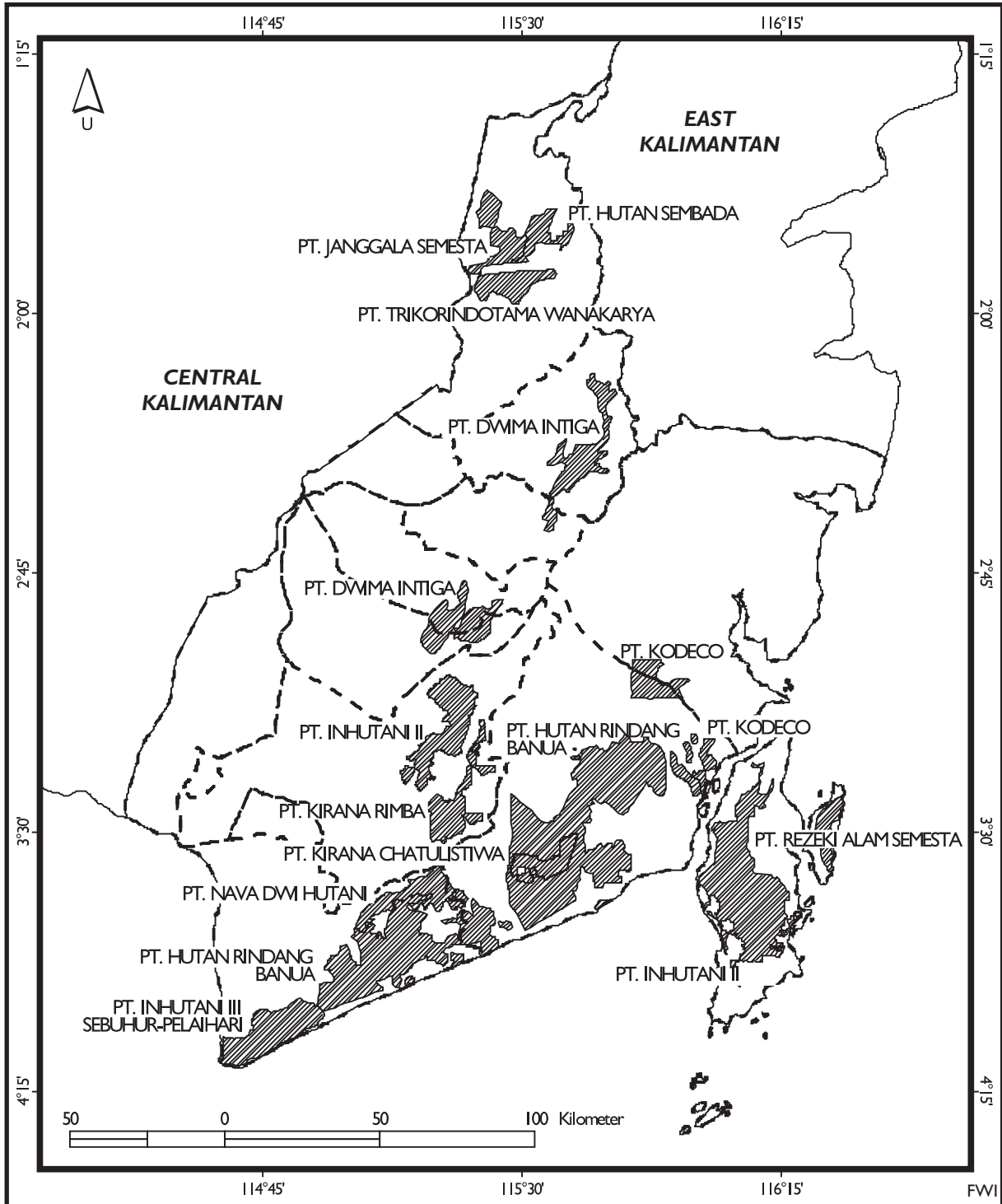


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| ■ MALAYSIA | ■ BANGLADESH |
| ■ MAURITIUS | ■ BRITISH VIRGIN ISLAND |
| ■ CAMBODIA | ■ INDONESIA |

APPENDIX 2: FOREST COVER IN SOUTH KALIMANTAN



APPENDIX 3: INDUSTRIAL TIMBER PLANTATIONS IN SOUTH KALIMANTAN



APPENDIX 4: NGO LETTER TO INVESTORS

Sent November 2005

To:
Raiffeisen Zentralbank
z.H. Gen.Dir. Dr. Walter Rothensteiner
Am Stadtpark 9
A-1030 Wien
walter.rothensteiner@rzb.at
andreas.ecker@rzb.at

To:
Andritz AG
z.H. CEO Dr. Wolfgang Leitner
Stattegger Straße 18
A-8045 Graz
wolfgang.leitner@andritz.com
michael.buchbauer@andritz.com

Re: Concerns regarding the United Fiber System pulpmill and wood chip mill in Indonesian Borneo (South Kalimantan)

Dear Mr. Leitner and Mr. Rothensteiner,

We, the undersigned, are deeply concerned about the involvement of your respective companies in the proposed construction of a huge pulp mill and of a wood chip mill by the company 'United Fiber System (UFS)' in South Kalimantan, Indonesia. Andritz AG has signed a contract with UFS to supply the main machinery with a value of more than US\$250 million and RZB is financing US\$21 million or 53% of the wood chip mill.

A new pulp mill and wood chip mill must be viewed in the context of the forest situation in Indonesia. Currently, there is tremendous overcapacity in the pulp industry and rampant illegal logging. Government policies specify that timber for the pulp industry should be produced in plantations, and should not originate from natural forest cover. For the most part, this has not been the case, as the pulp companies have expanded their capacities and focused on wood procurement from natural forests instead. Approximately 75-80% of wood used in pulp industry in Indonesia originates in natural forests, and recent reports by international research agencies and international donors have indicated that the majority of timber harvested from Indonesia's forests up to 73% -- is illegally logged.

As long as the rate of deforestation and associated illegal logging caused by the pulp industry due to rampant overcapacity in the sector has not been eliminated, any investment in a new pulp mill would only compound the structural problems of overcapacity and deforestation.

Every major pulp mill in Indonesia has caused either major social problems, pollution or deforestation - in most cases all of these. Research indicates that the proposed pulp mill in South Kalimantan will be no

Independent research institutions -- CIFOR [2005], Jaakko Pöyry [2004], GLOBAL 2000 [2005] have found that there is insufficient plantation land available in South Kalimantan to sustainably supply the pulp mill and the wood chip mill with fibre wood. The latest analyses indicate that UFS lacks at least 133,000 hectares of plantation land needed to produce the volume of fibre wood required to feed the two mills. Within the concession area of UFS alone there are 73,000 ha of highly endangered natural forest, and the wood chip mill threatens another 40,000 ha of precious lowland forests. As UFS frankly admits, an expansion of the facility's capacity to 1.2 million tonnes of pulp production per year is projected for the near future. A sustainable fibrewood supply of 6 million m³ of plantation wood per year would be needed for such a capacity. There is no way to provide such a supply without destroying additional natural forest.

Furthermore UFS states in their Environmental Impact Analysis (EIA) recently leaked to the public, despite efforts by UFS to keep the report secret, that a complete loss of aquatic sea life in the area of the pulp mill is to be expected, resulting in the loss of hundreds of livelihoods in traditional fishery. Also a massive regional increase in acute respiratory diseases as well as skin diseases and malaria is forecasted in the company's EIA. The construction of the deep sea port for the wood chip mill will destroy rare and precious mangrove forests and will significantly harm the aquatic sea life in the area.

We, the undersigned, are of the opinion that European companies with a reputation of being environmentally aware and of acting in a responsible manner should not get involved in industrial projects like this one. As a signatory of the "UN Environmental Programme Finance Initiative" Raiffeisen Zentralbank has a commitment to prevent environmental damage and to apply the precautionary approach. We therefore urge the bank to act according to its international commitment. Andritz AG is a global leader in pulp and paper technology and has in the past supplied machinery to several controversial and destructive pulp mills in Indonesia and in other parts of the world. This time, Andritz should take the long-term effects of the project concerned into consideration and refrain from supplying equipment to United Fiber System. The proposed UFS pulp mill and wood chip mill do not contribute to the sustainable development of Indonesian Borneo, but, on the contrary, contribute to widespread deforestation, and to a further degradation of nature and human living conditions in the region.

Currently, your two companies are set to play a leading role in the massive, and potentially illegal, destruction of Indonesia's remaining forests. We therefore urge you to carry out appropriate due diligence and withdraw from the projects concerned.

Sincerely,

[petition signatories]

APPENDIX 5: NGO LETTER TO INVESTORS

(A letter from a local environmental activist to the Banjarmasin Post newspaper)

The post-Soeharto reform era, from 1998 onwards, brought several government policy changes including a new Forestry Law (No.41/1999). This states that the public is allowed to know about "plans for forest zoning, forest exploitation and other forestry information." (Clause X, Paragraph 68, Article 2 on Community Participation).

The South Kalimantan provincial government's policy of denying people the opportunity to obtain information about forestry is exactly the opposite.

The only information given to local people so far is that a US\$1.2 billion (Rp12 trillion) pulp and paper plant will be built in South Kalimantan, as result of the provincial governor's visit to the 2000 World Expo in Hannover, Germany. At a public meeting on pulp and paper at his office on May 15th 2002, the South Kalimantan governor explained that the pulp mill would increase state revenues (*Bpost* 16/5).

The (then) head of the provincial forestry service, Sony Partono, said separately that his office had identified a source of raw materials for the paper pulp mill (*Bpost* 24/4). This was to be the HTI plantation concession of PT Hutan Rindang Banua (formerly PT Menara Hutan Buana) (*Bpost* 14/11).

The Forestry Law paragraph quoted above means that all layers of the South Kalimantan provincial government are obliged to provide information about forestry planning in South Kalimantan.

The reality is, sadly, very different. When I asked the Regional Investment Planning Agency (*BKPM*) for information about the investors backing the pulp project and PT HRB, the response was that this would need the office head's approval because pulp and paper had become a political issue.

This was rather confusing: what had been politicised? Two spokespeople to whom the *BKPM* referred me also used this 'political' excuse to block information requests about investors.

Similarly, a spokesperson for the South Kalimantan provincial forestry service said that the office did not have a profile of PT HRB because this information had not been made available to them (i.e. some higher authority has not released it for public use yet).

What really lies behind the South Kalimantan administration's ignorance?

The government always stresses the importance of community involvement but, by refusing local people access to information, it is infringing the national Forestry Law and denying us a role in the development of our beloved province.

Source:
Banjarmasin Post, 20 January 2003

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“Besides operating within international environmental standards and ensuring a sustainable supply of wood raw material to our mills from well managed forest plantations, we are resolute in supporting the economy And social environment within the local communities.

We are also committed to preserving the natural forest with high biodiversity value and to exclusively use plantation wood in our mills.”

**Kishore Dass
(then) UFS Chief Executive Officer**

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