No. 01, 2013

POLICY BRIEF

Strengthening Evidence-Based and Progressive Policy Reform

Encouraging Transparency of Forestry State Revenue

(Program: Working toward Including Forestry Revenues in the Indonesia EITI System)

by:
Article 33 Indonesia[1]

NORWEGIAN EMBASSY

Supported by:
The Royal Norwegian Embassy

Main Findings

- State loss due to illegal logging is Rp 30.3 trillion per year.
- Realization of Forest Resource Rent Provision (PSDH) revenue from legal timber is only 30% of its potential.
- The EITI and SVLK scheme can be implemented synergistically to promote transparency of forestry sector revenue, as an initial step to improve forestry sector governance.

Background

The forestry sector is an extractive industry with very high revenue loss in Indonesia. The results of research on 2003-2006 periods indicate that the state loss due to illegal logging is between US$ 2-3 billion per year.[2] This is supported by the findings of the Supreme Audit Agency (BPK) RI in 2010 that the

1 Written by Riko Wahyudi and Sonny Mumbunan, translated and edited by Kanti

2 World Bank (2006), *"Sustaining Indonesia's Forests: Strategy for the World Bank 2006-2009."* Jakarta: World Bank.

state loss due to illegal logging is Rp 83 billion per day or Rp 30.3 trillion per year. As much as 70-80% of log production in Indonesia is estimated to come from illegal timber.[3] Meanwhile, the formal forestry sector contribution to Gross Domestic Product (GDP) is not more than the range of 1% or US$ 1.8 billion per year over the last decade, according to the Central Statistics Agency (BPS) in 2012.[4]

Forestry sector's contribution to GDP is very small when compared to the potential of forest area in Indonesia which reached 136.88 million ha.[5] As an illustration, Indonesian forest area is equivalent to 61% of its land area or a combination of the UK, Germany, France, and Finland put together. About 60% of the total forest area is production forest (82.38 million ha). In this production forest area, forest resource extraction activities take place on a large scale, both timber and non-timber. Currently, the utilization of forest in the form of Timber Utilization permit (IUPHHK) in production forest has reached 35.38 million ha or approximately 49.93%.[6]

From the extraction of forest resources, the government obtained Non-Tax State Revenue (PNBP) of Forest Utilization Permit Fee (IIUPH), Forest Resource Rent Provision (PSDH), and the Reforestation Fund (DR). *IIUPH* and *PSDH* levy are imposed on timber and non-timber production from natural forests and plantation forest, while the DR levy is imposed only on timber production in natural forests. The following analysis focuses on state revenues from timber harvesting. Largest share of *PNBP* is derived from the *PSDH*, *DR*, and *IIUPH* levy, which are then distributed to the producing region.[7] Three issues to be observed in this policy brief are: (1) the forestry sector revenue stream, (2) loss of forestry sector revenue, (3) the mechanism of transparency in the forestry sector.

The Forestry Sector Revenue Stream

Based on the forestry statistical data 2011, non-tax state revenue (PNBP) from the forestry sector has increased in the last three years (Figure 1). Yet, this increase is not significant and is still low when compared to *PNBP* from the forestry sector in 2004 which reached Rp 3.42 trillion. Forestry sector *PNBP* with all the potential of Indonesian forests only range between USD 2-3 trillion per year.[8] In fact, the number has been derived from both timber and non-timber harvest revenue.[9]

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3 L. Tacconi (2007), "*Verification and certification of Forest Products and Illegal Logging in Indonesia*." London dan Sterling: Earthscan.

4 Nurrochmat and Hasan (2010), "*Ekonomi Politik Kehutanan: Mengurai Mitos dan Fakta Pengelolaan Hutan.*" Jakarta: INDEF.

5 Kementerian Kehutanan (2012), *"Statistik Kehutanan 2011."* Kementerian Kehutanan.

6 *Ibid.*

7 Biro Keuangan Kementerian Kehutanan (2012), *PNBP Sumber Daya Alam Kehutanan*. Presentation material in National Forestry FGD held by Article 33 Indonesia, March 8, 2012.

8 *Ibid.*

9 The Non-Tax State Revenue (PNBP) of timber consist of: Reforestation Fund (*Dana Reboisasi/DR*), Forest Resource Rent Provision (*Provisi Sumber Daya Hutan/PSDH*), Forest Utilization Business Permit Fee (*Iuran Izin Usaha Pemanfaatan Hutan/IIUPH*), Stumpage Value Compensation (*Ganti Rugi Nilai Tegakan/GRNT*). Meanwhile, non-timber *PNBP* consist of: Forest Exploitation Violation Fines (*Denda Pelanggaran Eksploitasi Hutan/DPEH*), Forest Area Utilization (*Penggunaan Kawasan Hutan/PKH*), Natural Plant Hauling Fee (*Iuran Mengangkut/Tumbuhan Alam Hidup atau Mati/IASL/TA*), Concession for Nature Tourism Permit Fee (*Pungutan Izin Pengusahaan Pariwisata Alam/PIPPA*), Nature Tourism Object Entrance Fee (*Pungutan Masuk Obyek Wisata Alam/PMOWA*), and Concession for Nature Tourism Profit Fee (*Iuran Hasil Usaha Pengusahaan Pariwisata Alam/IHUPA*).

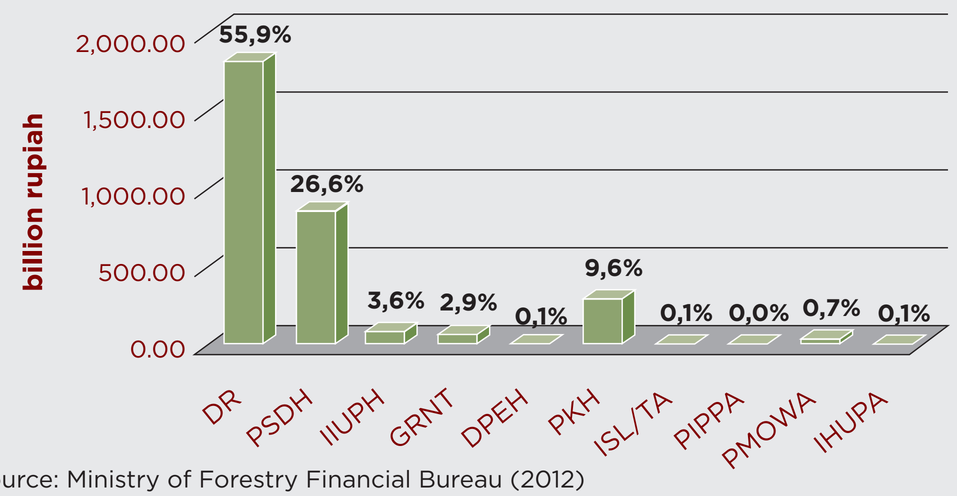
Figure 1
Forestry Non-Tax Revenue 2006-2011

Source: Ministry of Forestry (2012)

Note: PNBP= *Penerimaan Negara Bukan Pajak* (non-tax state revenue)

Nearly 90% of non-tax revenues derived from timber non-tax revenue, in the form of *DR, PSDH, IIUPH, GRNT* (Figure 2). This suggests that timber extraction is still a major source of state revenue from the forestry sector. Of the four instruments of the timber non-tax revenues of wood, three instruments are allocated and distributed to the producing areas through revenue-sharing fund schemes (DBH). The three instruments of Forestry Natural Resource revenue-sharing fund is the *DR*, *PSDH*, and *IIUPH*. *GRNT* is not allocated to the producing area.

Figure 2.
Forestry Sector Non-tax State Revenue 2011



Source: Ministry of Forestry Financial Bureau (2012)

Note: DR=*Dana Reboisasi*/Reforestation Fund; PSDH=*Provisi Sumber Daya Hutan*/Forest Resource Rent Provision; IIUPH=*Iuran Izin Usaha Pemanfaatan Hutan*/Forest Utilization Business Permit Fee; GRNT=*Ganti Rugi Nilai Tegakan*/Stumpage Value Compensation; DPEH=*Denda Pelanggaran Eksploitasi Hutan*/Forest Exploitation Violation Fines; PKH=*Penggunaan Kawasan Hutan*/Forest Area Utilization; ISL/TA= *Iuran Mengangkut/Tumbuhan Alam Hidup atau Mati*/Natural Plant Hauling Fee; PIPPA=*Pungutan Izin Pengusahaan Pariwisata Alam*/Concession for Nature Tourism Permit Fee; PMOWA=*Pungutan Masuk Obyek Wisata Alam*/Nature Tourism Object Entrance Fee; IHUPA=*Iuran Hasil Usaha Pengusahaan Pariwisata Alam*/Concession for Nature Tourism Profit Fee.

Allocation of Forestry Resource *DBH* generally depends on three principles: first, the derivation principle where *DBH* is distributed to the producing region. Second, the realization principle where *DBH* distributed to regions based on the realization of non-tax revenues. Third, the equal share principle where *DBH* is also distributed evenly proportioned to other non-producing areas in the producing provinces.[10]

The three principles can be observed particularly in the *PSDH* allocation. Under Regulation no. 55/2005 on Balancing Fund, the allocation of *PSDH* fund is 20% for the central government, 16% for province-producing regions, 32% for producing regency/municipality, and 32% for regency/municipality in the respective province. As for *IIUPH*, the allocation is 20% for the central government, 16% for the province, and 64% for producing regency/municipality. Especially for *DR*, the allocation is only by 60% for central government and 40% for producing regency/municipality (Table 1).

Table 1
Forestry Resource Revenue-Sharing Fund Balance

No	Revenue-Sharing Fund source	Allocation of Revenue-Sharing Fund			
		Central	Province	Producing Regency/ Municipality	Other Regency/ Municipality in respective Province
		(%)	(%)	(%)	(%)
1	Forest Utilization Business Permit Fee (*IIUPH*)	20	16	64	-
2	Forest Resource Rent Provision (*PSDH*)	20	16	32	32
3	Reforestation Fund (*DR*)	60	-	40	-

Source: PP no. 55/2005

PSDH and *IIUPH* fund can be distributed by the local government for regional development in general. Meanwhile, specific to the *DR*, its distribution is required for the rehabilitation and reforestation of land. Under Regulation no. 35/2002 on the Reforestation Fund, *DR* share of the producing regency/municipal (40%) is distributed for rehabilitation and reforestation of land in forest areas 60% and land outside the forest area 40%.

10 S. Mumbunan (2012), "Dana Bagi Hasil Kehutanan dan REDD+." Presentation material on training Policy Analysis for REDD+ Within a Decentralized Context, cooperation of Research Center on Climate Change University of Indonesia and Crawford School of Public Policy Australian National University, Jakarta, August 7-10 2012.

Loss of State Revenue from Forestry Sector

Forestry sector non-tax revenue is small when compared with other extractive industries. Non-tax revenue from general mining sector, for example, in the year 2011 reached Rp 24.24 trillion.[11] The amount of revenue is relatively large when compared with the forestry tax revenues that is only around Rp 3 trillion per year.[12]

When examined, the loss of state revenue from the forestry sector is very high. One was due to illegal logging. In 2003, research result from Brown (2009) and Greenpeace (2003) showed about 50 million m3 or 70% of log production Indonesia is illegal. This is consistent with other research, including the findings of BPK RI in 2010 mentioned above.

Based on the above data and information, it can be estimated that the legal log production in Indonesia is only about 30% of the total log production. When the 30% proportion is juxtaposed with the realization and the potential for legal timber *PSDH*, we obtain quite surprising results. Article 33 Indonesia calculations show that the realization of the *PSDH* value from legal timber in 2009 and 2010 are only about 30% of the supposed potential (Table 2).[13] The *PSDH* realization value use figures of *PSDH* forecast allocation in the Minister of Finance Regulation on Forestry resource. Meanwhile, the potential value use official data of timber production from the Ministry of Forestry. In other words, the state can still get potential revenue of 70% of the legal timber *PSDH* value.

Table 2
Comparison of Forestry PSDH allocation and Legal Timber PSDH Value Simulation

Year	PSDH for Timber and Non-Timber PNBP (billion Rp)	Potency of Timber PSDH (billion Rp)	Comparison of Realization and Potency (%)
2009	699,3	2.115,6	33,1
2010	597,1	2.470,9	24,2

Source: Simulation Result by Mumbunan and Wahyudi (2012)

The above data only explain the state loss from timber production sector alone, not including non-timber forest products such as rattan, honey, silk, rubber and so on. In addition, there are also informal levies by various government actors along the value chain of forest resource extraction. One informal levy, by some, is called “entertainment fee” for smooth business in the forestry sector.

11 Kementerian Energi dan Sumber Daya Mineral (2012), “Laporan PNBP Pertambangan Umum 2012.” Jakarta: Kementerian Energi dan Sumber Daya Mineral Republik Indonesia.

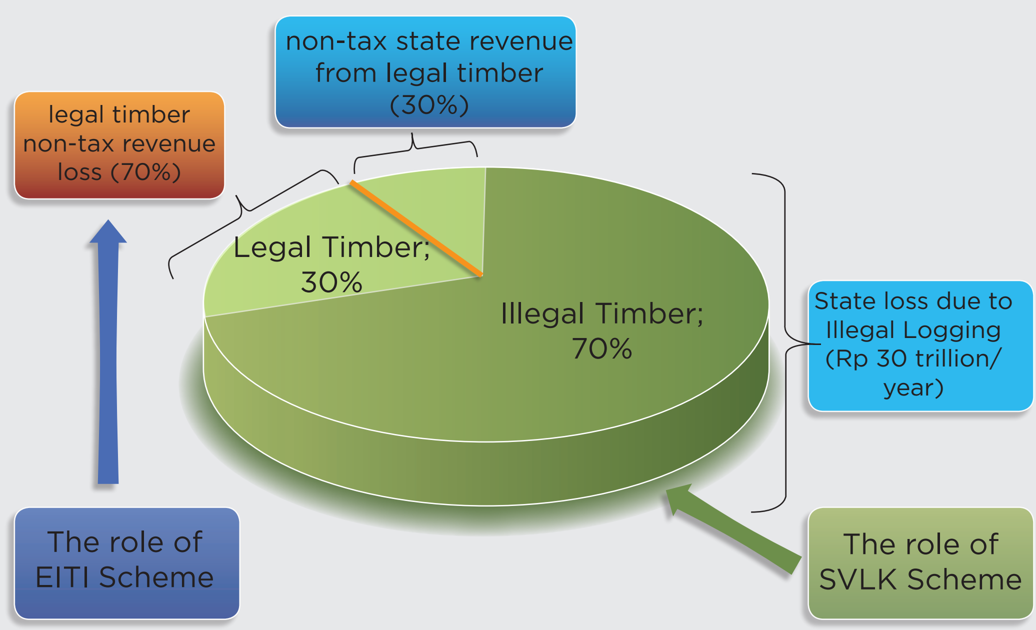
12 Kementerian Kehutanan (2012), “Statistik Kehutanan Indonesia 2011.” Jakarta: Kementerian Kehutanan Republik Indonesia.

13 S. Mumbunan dan R. Wahyudi (2012), Transparansi Penerimaan Industri Ekstraktif Sektor Kehutanan di Indonesia. Laporan Studi Pelingkupan. Jakarta: Article 33 Indonesia.

Transparency Mechanism in the Forestry Sector

The high loss of state and local revenue from the forestry sector requires governance improvement. One is through the mechanism of transparency. Transparency could be the first step to improve forestry sector governance as a whole. Currently, there are several schemes of transparency with multi-stakeholder engagement that can be applied in the forestry sector, mainly to prevent the high loss of state revenue. Two of them are Timber Legality Verification System (SVLK) scheme which entered into force and mandatory in the forestry industry and the Extractive Industries Transparency Initiative (EITI) scheme. Related to the forestry sector state revenue, the *SVLK* conceptually scheme targets legality of the timber including its revenue. The revenue is valid for legal timber and expected to later include illegal timber that decided to join the *SVLK* scheme. While the EITI scheme targets the revenue of legal timber.

Figure 3
Revenue Loss from Timber and the Role of EITI and SVLK Scheme



Source: Self-production (2012)

SVLK scheme ensures that the timber industry, including *IUPHHK*, get wood or other materials through a legal way from a system of sustainable management of natural resources, which heed legality, and sustainable forest management. One of the criteria of the verification standard in *SVLK* is fulfilling the government levies payment obligations and the validity of the transport timber, especially *PSDH* and *DR*. In the *SVLK* scheme verification is conducted by an independent verification agency and can be monitored by the public. *SVLK* can save forests and state revenue due to illegal logging if implemented appropriately. Therefore, the implementation of *SVLK* needs support and supervision of the various stakeholders in the forestry sector.

Meanwhile, the EITI is a global initiative that aims to promote transparency and accountability in the extractive industries sector revenues, with the publication of data on government revenue and data on company payment, to be reconciled independently. Currently, Indonesia is the candidate country to meet the requirements of EITI. Extractive industries sector that have been included in the scoping EITI Indonesia are only mining, oil, and gas.

Currently, the forestry sector has not been included in the scope of EITI. Article 33 Indonesia through the support of the Embassy of the Kingdom of Norway is encouraging the entry of the forestry sector in Indonesia EITI scheme. EITI is important in the forestry sector to save the state non-tax revenue loss from legal timber payments by the company. EITI mechanism, for example, will be able to compare the information on the volume of timber and contribution of legal timber non-tax state revenue from the company received by the Government. In the end, this will ensure that 70 percent of state revenue is received in the state treasury. In the review above, if 70 percent of legal revenue can be received by the state treasury, the contribution of non-tax state revenues of the forestry sector will be almost equivalent to the mining sector. Therefore, this transparency is very important to be implemented in Indonesia. As is for the *SVLK* scheme, the EITI mechanism will require multi-stakeholder support.

Starting from the above description, the EITI scheme can be implemented in line along with *SVLK* schemes in the forestry sector.

Conclusion

Loss of state revenue from the forestry sector is very high. Of the total log production Indonesia, 70% is from illegal logging. State losses from illegal logging have reached Rp 30.3 trillion every year, plus loss of revenues from legal timber. Article 33 Indonesia simulation result shows the state lost about 70% of the legal timber *PSDH* fees.

Improvement of forestry governance is very important, one of which begins with concession transparency. EITI scheme that encourages transparency of company payments and government revenues are particularly relevant to save non-tax state revenues from the forestry sector legal forest products. Meanwhile, *SVLK*, which aims to ensure the timber from the forest is legal, could also be encouraged for state revenue transparency, in addition to preventing illegal logging. EITI and *SVLK* scheme can be implemented in synergy to improve forestry sector governance.

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