

TOO LITTLE TOO LATE



The failure of Japan's housing industry supply chain to take effective action on the devastation of tropical forests and human rights, especially in Sarawak.

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Markets For Change is a market-focused eNGO. Its mission is to drive responsible industry and business practices through an informed public which has the power to change markets and public policy.

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JATAN is a Japanese NGO, which is committed to the conservation of tropical rainforests and forests all over the world.

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▶ EXECUTIVE SUMMARY

In February and March of 2016 Markets for Change and JATAN produced a report 'Forest to Floor: How Japan's Housing Construction is Driving Forest Destruction and the Dispossession of Indigenous People in Sarawak'. We circulated this report to all companies we had identified in the supply chain, held seminars in Tokyo and Osaka for company representatives, and also met with a number of companies separately to discuss the issues with their timber supply originating in Sarawak, Malaysia. During the year we supplied several updates on relevant issues to companies for whom we had appropriate contact information.

This report evaluates the response to our campaign of Japanese companies in the supply chain for plywood flooring. We had requested them to identify and cease procurement of timber products from Sarawak until such products can be independently verified as legal, sustainable and free from corruption and human rights violations. We also asked these companies to act in relation to timber from all sources by conducting robust due diligence analysis on their supply chains to ensure that corruption, illegal logging, human rights violations, and environmental degradation are not associated with the timber they buy, and to immediately cease sourcing where this cannot be guaranteed.

The overwhelming majority of the 67 companies that received our follow up questionnaire in December 2016 are unwilling to engage on the issues, yet it is understood that for all companies Sarawak product is present in a significant proportion of plywood flooring they handle.

Most are not transparent about their policies and practices. This failure to answer questions regarding the environmental and human rights attributes of their wood supply indicates an unwillingness to expose poor practices to public scrutiny. A number outlined that supply contracts forbid them from revealing the identity of the company from whom they buy – an unacceptable requirement under modern practice that regards knowledge and public exposure of chain of custody as a fundamental requirement.

Of those 18 companies that did answer our questions not one company has excluded Sarawak wood from their supply chain.

All the companies continue to play a role in the devastation of Sarawak's environment and dispossession of indigenous people because they buy product in which timber originated from Sarawak. Their demand for timber is driving the unacceptable practices.

Despite evidence to the contrary over many years and the restricted scope of recent efforts to rein in illegal practices, most companies claim to expect a gradual improvement from this source over time – mostly leaving responsibility for any such improvement with the companies who currently supply them and therefore have a vested interest in the status quo. This is an unrealistic scenario.

Some companies explicitly place financial considerations above ethical responsibility.

All companies are ignoring the urgency of the situation in Sarawak – where there may be as little as five years left before the annihilation of that part of the Heart of Borneo located in Sarawak. They also ignore that it is a special case more extreme than other sources in terms of rampant corruption, illegal logging, dubious standards of legality and acute environmental and social impacts.

Regarding the development of responsible procurement policies generally, Japanese companies lag far behind those in other developed countries. Only a handful have attempted to develop policy on environmental matters and human rights issues as part of their procurement regime, with only one company assessed as comprehensively addressing these vital matters.

Most companies are failing to act to improve their existing procurement guidelines, if they even have any such guidelines relating to the issues.

Companies are awaiting the development and implementation of regulations under Japan's new Clean Wood Act of 2016. The legislation fails to mandate that all companies trade only in legal product and is therefore seriously deficient compared to legality measures elsewhere in developed countries. There is no prohibition against trading in illegal timber, and no penalties for doing so. Companies may choose whether or not they will implement standards for procurement of legal timber. It is unclear whether those standards, which are still being developed at the time of writing, will be weak or strong.

Many companies may not even bother to meet the deficient new law, as adherence is voluntary. We understand that the industries importing wood and utilising wood from overseas are currently lobbying for minimal standards. The Sarawak Timber Association (STA) has also been lobbying in Japan for the continuance of the trade without the constraints that improved standards would deliver.



▶ CONCLUSION

The failure of Japanese housing and condominium companies in the supply chain of plywood flooring from Sarawak to take responsibility for their crucial role in driving destruction of natural forests and dispossession of indigenous people in that Malaysian state is extremely disappointing and concerning. It is below international norms for developed countries and exposes their customers to unacceptable product.

At the broader level of general procurement policy, the vast majority of companies are unwilling to be transparent and expose their practices to our independent expert third party assessment. We understand that this is because of their serious policy deficiency on environmental and social issues associated with the forest products in which they trade.

Whilst we congratulate the handful of companies that are more advanced and responsible in their attitude and willing to answer our questions and discuss the issues, they fail to yet meet the minimum standards of the rest of the developed world, with few exceptions.

An approach of incremental improvement without timelines, enforcement, assessment of effectiveness, or reassessment of whether issues are covered appropriately, comprises greenwashing more than it represents genuine effort.

Recent legislation falls short of mandating that companies must not trade in illegal timber.

RECOMMENDATIONS:



1. **Japanese companies in the housing industry supply chain** for plywood flooring products now apply the recommendations of our 2016 report to;

- identify and cease procurement of timber products from Sarawak until such products can be independently verified as legal, sustainable and free from corruption and human rights violations, and
- conduct robust due diligence analysis on their supply chains to ensure that corruption, illegal logging, human rights violations, and environmental degradation are not associated with the timber they buy, and to immediately cease sourcing where this cannot be guaranteed.



2. It is time for **concerned citizens and consumers** to become involved in urging change if natural treasures, human rights and traditional lifestyles and livelihoods are not to be lost forever. See the Markets For Change and JATAN websites for further information on how to contact companies.



3. **Investors in companies participating in Japan's housing industry supply chain** should also ensure that those companies apply high procurement standards such as those operating in other developed countries. In this way investors can contribute to a positive outcome to the current unacceptable situation, and ensure that their own investment reputation on environmental and social standards is not jeopardised.



► INTRODUCTION

This report assesses the performance of Japanese companies in the supply chain from Sarawak on the implementation of procurement guidelines to protect environmental values and human rights.



Our last report, *'Forest to Floor: How Japan's Housing Construction is Driving Forest Destruction and the Dispossession of Indigenous People in Sarawak'* was published in March 2016. It was the result of extensive research, plus questionnaires and meetings with Japanese companies, and found that companies needed to take immediate action to stop the ongoing destruction of Sarawak's forests and dispossession of indigenous people. After producing the report, we met

with Japanese companies again and conducted seminars for companies to try and persuade them that they should immediately stop the procurement of timber products from Sarawak.

This report is an update on companies' progress in the 9 months since our report was produced. It is in part the result of another new questionnaire we sent to Japanese companies which surveyed them on a range of subjects including environmental concerns, social issues, scope of procurement policies and questions specific to the trade of timber products from Sarawak. It finds that while a small number of companies have made some progress, the majority remain inactive on the issue of Sarawak, and more generally on the issue of developing acceptable procurement policies.

► JAPAN – SARAWAK SUPPLY RELATIONSHIP

Trade Volumes and Value

Japan imports approximately three quarters of its wood supply.¹ Recent reports and studies from various NGOs list Malaysia, Russia (via China) and Romania as some of the high-risk countries from which Japan imports wood and forest products.²

Plywood and sawn wood account for the bulk of Malaysia's timber exports. The majority of plywood is produced in the state of Sarawak, the state of Malaysia with the most seriously unacceptable logging regimes, regarded as high risk. It comprises about 70 per cent of total Malaysia's total production.

Japan is the major consumer of plywood products from Sarawak. In 2012, plywood exported from Sarawak, Malaysia comprised 49% of Japan's entire plywood import.³ In January to September 2016, Japan was still the number one importer of plywood from Sarawak with the statistics now showing 56% of the export volume (715,995 m³) valued at RM1.3 billion⁴. In 2017 Japan remained the single largest importer of ply products from Sarawak with latest figures also at 56% of all plywood produced in Sarawak.⁵

90% of plywood in Japan is used in the housing sector.⁶ While the majority of plywood imported from Malaysia is for concrete formwork, a significant proportion is for use in flooring.

Supply Chain

Timber is harvested and exported from Sarawak by several major logging companies known as the 'Big 6'. These are Samling, Shin Yang, Ta Ann, WTK, Rimbunan Hijau and KTS.

Major Japanese trading houses importing Sarawak timber products include Itochu Kenzai Corporation, Sumisho & Mitsuibussan Kenzai (SMKC), Sojitz Kenzai, Marubeni Kenzai, Toyo Materia and Sumitomo Forestry. A merger was recently announced between Sumisho & Mitsuibussan Kenzai and Marubeni Building Materials Ltd, effective 1st January 2017.⁷

The product is then distributed to major flooring manufacturers and to wholesalers of building material including: Daiken, Eidai, Panasonic, Noda, Asahi Woodtec, Wood One, Japan Kenzai co. Ltd, Nice Corporation and Jutec Corporation. See our 2016 report for an outline of the plywood flooring supply chain structure.⁸

Japanese trading companies tend to have business partnerships / shareholdings with specific logging companies in Sarawak and vice versa. This interest allows for vertical integration of the supply chain, leaving Japanese companies with significant influence over logging companies in Sarawak. This arrangement is evident Daiken's business relations, for example: Daiken receive timber products from their own plantations and directly from a number of Sarawak logging companies including Samling and KTS. The rest of the timber product is supplied to Daiken by Itochu Kenzai Corporation. Itochu Corporation has a 26.5% stake in Daiken. And Daiken have a long standing interest in Samling.

At the end of the supply chain are housing companies and condominium developers. These companies have a direct relationship with the public, for whom they build. It is vital that their claims to eco-credentials extend to the timber products used in the floors of their buildings. Currently this is not the case. Material from Sarawak is present in the supply of all such companies and will therefore appear in buildings for which they are responsible. We believe that consumers would be disappointed by such complicity in driving destructive logging.



► OUR QUESTIONNAIRE

In December 2016, Markets For Change and JATAN sent a comprehensive questionnaire to 67 Japanese housing and condominium construction companies, trading houses and flooring manufacturers. (This questionnaire can be found on the Markets For Change and JATAN websites: www.marketsforchange.org/FTF_questionnaire <http://www.jatan.org/archives/3720>) . The questionnaire sought to establish if any progress had been made in relation to the development of procurement policies, whether any action had been taken to stop the procurement of timber products from Sarawak and whether the companies has any process to investigate their supply chains and to implement changes and reviews to procurement policies.

We asked specific questions regarding procurement policy in a number of fields. These were Environmental, Social, Scope of Procurement Requirements and Sarawak. They were broken down as follows (these criteria are the same as, or similar to, those applied by other NGOs):⁹

Environment

- Is the degradation or conversion of natural forests prohibited?
- Are forestry operations in primary forest prohibited?
- Are forestry operations that degrade high carbon value and/or high carbon stock forest prohibited?
- Are operations in protected areas prohibited? Are harvestings of protected species prohibited?
- Do you require proof of legality in sourcing and operations?

Social

- Do you require proof of legality in sourcing and operations?
- Is a check of land tenure required?
- Is proof of free, prior and informed consent of indigenous communities required where applicable?
- Is there any check on whether concession issuances and wood products are tainted by corruption?

Scope of Procurement Requirements

- Existence of policy – does the company have a procurement policy in place?
- Comprehensiveness – if so, how comprehensive is the policy? Does it cover a range of relevant environmental and social concerns?
- Transparency - public availability of information
- Review and verification – Is there a process to review and verify the implementation and application of the policy?
- Improvement – Is there a process in place to improve the policy?
- Implementation – is there a process to implement the policy?
- Independent advice on policy development – does the company seek independent advice on the development and improvement of procurement policies?
- Certification requirement – does the policy preference reliable certification schemes?

Sarawak

- Did your company investigate your supply chain for wood products originating from Sarawak?
- Did your company find wood products originating from Sarawak?
- In relation to Sarawak specifically: Have you proven "legality" with document(s) issued by Sarawak State Government?
- Do you regard such a document as sufficient to prove 'legality'?
- Did your company stop procurement from Sarawak?

► COMPANY RESPONSES

The findings are summarised and the performance of companies is assessed in the 'Failure to Answer' diagram (see right) and the 'Procurement Policy Assessment' chart on the next page.



Failure to Answer

*** A further 4 companies** each provided a generalised reply that did not address the specific questions and criteria. **One other**** provided answers that were incomprehensible and insufficient to outline their policies. These have also been assessed at zero for the entire exercise. These companies are also believed to continue to receive wood supply originating in Sarawak.

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*** Of the 67 companies surveyed, 44 did not provide any response despite several communications** following up on the distribution of the questionnaire. This failure to provide any information is assessed negatively. As no evidence has been provided of policy in relation to the specific criteria put to companies we score the response as zero for each question. We understand that all of these companies continue to receive plywood of Sarawak origin.

Procurement Policy Assessment Summary and Key.

PROCUREMENT POLICY ASSESSMENT SUMMARY	ENVIRONMENT					SOCIAL				SCOPE OF PROCUREMENT REQUIREMENTS						SARAWAK					
	Degradation of natural forests	Forest operations in primary forests	Forest operations that degrade high carbon value forests	Forest operations in protected forests and protected species	Proof of legality in sourcing and operations	Proof of legality in sourcing and operations	Land Tenure Check	Proof of free, prior & informed consent from indigenous people	Checks re: issuance of wood products tainted by corruption	Existence of procurement policy	Comprehensiveness of policy	Transparency - Public availability of policy	Certification requirement	Independent advice on policy development	Review to verify implementation	Improvement to policy guidelines	Did your company investigate your supply chain for wood products originating from Sarawak?	Did your company find wood products originating from Sarawak?	In relation to Sarawak specifically: Have you proven 'legality' with document(s) issued by Sarawak State Government?	Do you regard such a document as sufficient to prove 'legality'?	Did you stop procuring timber products from Sarawak?
MISAWA	Green	Green	Green	Green	Green	Green	Green	Red	Red	Green	★★★★★☆☆	Green	Orange	Orange	Green	Green	Green	Red	YES	NO	Red
Daiwa House®	Green	Green	Red	Green	Green	Green	Red*	Red	Green	Green	★★★★★☆☆	Green	Orange	Green	Green	Green	Green	Red	NO	Red*	Red
SEKISUI HOUSE	Red	Green	Red	Green	Green	Green	Green	Red	Green	Green	★★★★★☆☆	Green	Orange	Green	Green	Red	Green	Red	NO	Red*	Red
ITOCHU	Red	Red	Green	Green	Green	Green	Green	Red	Green	Green	★★★★★☆☆	Green	Orange	Orange	Green	Red	Green	Red	NO	Red*	Red
LIXIL	Green	Green	Green	Green	Green	Green	Red	Red	Red	Green	★★★★★☆☆	Red	Green	Green	Red	Red*	Green	Red	YES	NO	Red
SUMITOMO FORESTRY CO.,LTD.	Orange	Orange	Orange	Orange	Green	Green	Red*	Orange	Red*	Green	★★★★	Green	Orange	Red	Green	Red	Green	Red	NO	Red*	Red
TOKYU LAND	Red*	Red*	Red*	Red*	Green	Green	Green	Green	Red*	Green	★★★★	Green	Red	Red*	Green	Red	Green	Red	YES	YES	Red
NODA	Red*	Red*	Red*	Green	Green	Green	Red	Red	Red	Green	★★	Red	Green	Red	Green	Red	Green	Red	YES	YES	Red
SEKISUI	Red	Red	Red	Green	Green	Green	Red	Red	Red	Green	★★	Green	Red	Red	Green	Red	Green	Red	YES	NO	Red
MITSUBISHI ESTATE	Red	Red	Red	Red	Red	Red	Green	Green	Red	Green	★★	Green	Green	Red*	Red	Green	Red	Red*	Red*	Red*	Red*
sojitz	Orange	Orange	Red*	Orange	Orange	Orange	Red*	Red*	Red*	Green	★★	Green	Green	Orange	Red*	Red*	Red*	Red*	Red*	Red*	Red*
AsahiKASEI 旭化成	Red	Red	Red	Green	Red	Red	Red	Red	Red	Green	★	Green	Red	Red	Green	Green	Green	Red	YES	YES	Red
DAIKEN	Red*	Red*	Red*	Red*	Green	Green	Red*	Red*	Red*	Green	★	Green	Orange	Red	Green	Red	Green	Red	NO	Red*	Red
PanaHome	Red	Red	Red	Red	Green	Green	Red	Red	Red	Green	★	Green	Green	Red	Green	Red	Green	Red	NO	Red*	Red
YKK AP	Red*	Red*	Red*	Red*	Green	Green	Red*	Red*	Red*	Green	★	Red	Orange	Red	Green	Red	Green	Red	NO	Red*	Red
WOOD ONE	Red	Red	Red	Green	Red	Red	Red	Red	Red	Green	★	Red	Orange	Orange	Green	Red	Red	Red*	YES	YES	Red*
Butsurin 物林株式会社	Red*	Red*	Red*	Red*	Red*	Red*	Red*	Red*	Red*	Red	X	Red	Red*	Green	Red	Orange	Green	Red	YES	Red*	Red
Butsurin 物林株式会社	Red*	Red*	Red*	Red*	Red*	Red*	Red*	Red*	Red*	Red	X	Red*	Red*	Green	Red	Red	Red	Red*	Red*	Red*	Red*



KEY: SCORING CRITERIA FOR PROCUREMENT POLICY ASSESSMENT SUMMARY



This indicates insufficient information or irrelevance in reply and has been scored as zero



ENVIRONMENT

Is the degradation or conversion of natural forests prohibited?	Degradation of natural forest is not prohibited	Some insufficient protections against conversion and logging of natural forests	Degradation or conversion of natural forests is Prohibited
Are forestry operations in primary forest prohibited?	logging in primary forest not prohibited	Some insufficient protections for primary forests	Operations in primary forests are prohibited
Are forestry operations that degrade high carbon value and/ or high carbon stock forest prohibited?	Not prohibited	Some insufficient protections for forest carbon	Prohibited
Are operations in protected areas prohibited? Are harvestings of protected species prohibited?	Not prohibited	Some insufficient protections	Prohibited



SOCIAL

Do you require proof of legality in sourcing and operations?	No	Implicitly through suppliers	Yes, explicitly in policy and conduct due diligence themselves
Is a check of land tenure required?	No	Implicitly through suppliers	Yes, explicitly in policy and conduct due diligence themselves
Is proof of free, prior and informed consent of indigenous communities required where applicable?	No	Implicitly through suppliers	Yes, explicitly in policy and conduct due diligence themselves
Is there any check on whether concession issuances and wood products are tainted by corruption?	No	Implicitly through suppliers	Yes, explicitly in policy and conduct due diligence themselves



SCOPE OF PROCUREMENT REQUIREMENTS

Existence of policy	Does not exist	In development	Exists
Comprehensiveness	This is assessed by range of issues covered, with one star being allocated for each issue covered: ★★☆☆☆☆		
Transparency - public availability of information	Not publicly available	Partial information available	Publicly available
Certification requirement	No certification requirements	Preferences certified timber products but does not differentiate between certifications	Preferences more reliable certifications and prioritises their procurement
Independent advice on policy development	No independent guidance	Use of unreliable/ unspecified advisors	Use reliable third party advice on development
Review to verify implementation	No substantive review process	Internal review	Regular third party review and verification
Improvement	No process for improvement	Internal process for improvement of policy	Consultative process for improvement of policy involving independent third party



SARAWAK

	YES/NO			
Did your company investigate your supply chain for wood products originating from Sarawak?		No		Yes
Did your company find wood products originating from Sarawak?		Yes		No
In relation to Sarawak specifically: Have you proven 'legality' with document(s) issued by Sarawak State Government?	Yes/No			
Do you regard such a document as sufficient to prove 'legality'?	Yes/No			
Did your company stop procurement from Sarawak?		No		Yes

► PROCUREMENT POLICY ASSESSMENT SUMMARY

The 18 companies that responded fully to the questionnaire have been assessed as described in the Procurement Policy Assessment Summary. It is clear that most of the companies who responded don't have sufficient processes in place to deal with the responsible procurement of timber. Many companies didn't have any procurement policies or guidelines, while some suggested they did but were unwilling to share any details.

A chart displays the relative scores of the different companies on the various criteria via a traffic light system of red, orange and green. This scoring methodology is described in the Assessment Scoring Criteria section.

We stress that these companies are more advanced and responsible in their attitude, being willing to answer our questions, discuss the issues and in some cases to apply improvements. However, they fail to meet the minimum standards of the rest of the developed world, with few exceptions. Not one company has excluded Sarawak wood from their supply chain. Several explicitly placed financial considerations above ethical responsibility.

A further 4 companies each provided a generalised reply that did not address the specific questions and criteria. One other provided answers that were incomprehensible and insufficient to outline their policies. These have also been assessed at zero for the entire exercise. These companies are also believed to continue to receive wood supply originating in Sarawak.

► MATTERS ARISING FROM COMPANY REACTIONS AND RESPONSES

The following section of this report discusses key issues and concerns arising from the survey and company attitudes.

Transparency

Transparency is a key factor in assessing a company's commitment to sustainable environmental and social practices. Companies who develop procurement policies must be prepared to make their policies publicly available so that consumers and trading partners can confidently assess whether the policies are sufficient.

Developing a culture of transparency is critical to the establishment of a genuine sustainable business practise and is critically important for companies who trade in high risk products, such as timber from developing and developed countries.

Transparency International described the importance of transparency in mitigating the risk of corruption and poor practice:

"Transparency is about shedding light on rules, plans, processes and actions. It is knowing why, how, what, and how much. Transparency ensures that public officials, civil servants, managers, board members and businesspeople act visibly and understandably, and report on their activities. And it means that the general public can hold them to account. It is the surest way of guarding against corruption, and helps increase trust in the people and institutions on which our futures depend"¹⁰

Both of our questionnaires asked direct questions about transparency, and in this report companies have been graded on their commitment to and practice of transparency (see 'Procurement Policy Assessment' chart). It needs to be noted that the only company that comes close to reaching acceptable transparent procurement policies that cover a broad range of social and environmental concerns was Misawa Homes. All the other companies that responded, even those with publicly available policies, fell short on a number of key policy issues.

A matter of great concern was that a number of companies said that they had confidentiality agreements with suppliers which prohibited them from making public the details of the source of timber products. Supply contracts forbidding companies from revealing the identity of the company from whom they buy are an unacceptable requirement under modern practice that regards knowledge and public exposure of chain of custody as a fundamental requirement.

Companies constrained by such provisions include Misawa Homes, which otherwise have a generally acceptable approach to the accessibility of their policies. This provides a considerable problem, considering that while they claim to have responsible guidelines in place, there is no way of checking this against their actual supply chain. Other companies that claimed to have such confidentiality agreements with suppliers explicitly requested that we did not identify them, which adds further to the problem of lack of transparency.

Some companies who responded to our questionnaire, did so without answering the specific questions that were asked. They did this by providing vague or irrelevant statements in the place of answers to specific questions. This obfuscation is important to note, because it reveals much about the companies'

lack of commitment to transparency and unwillingness to disclose details of their business practise which have a direct effect on the environment of Sarawak and the lives of indigenous people who are struggling for land rights and the right to protect the forest on which their lives, economies and culture depend. Some of the responses were so deliberately vague that it was impossible for us to assess their positions. These companies were marked on our 'Failure to Answer' diagram accordingly. They include Kajima Corporation, Asahi Woodtec, Daito Trust Construction, Toray Construction and Daikyo.

While it is understood that some information is 'commercial in confidence', the disclosure of which could have a negative impact on the capacity of companies to operate competitively, Markets For Change and JATAN is of the opinion that the questions we posed do not constitute this risk and that the failure of these companies to answer appropriately represents a considerable issue in relation to their commitment to good practice and transparency. We did not ask details of price, quantity, quality, or other such commercial arrangements.

Companies that trade in high risk products must be willing to hold their procurement policies and business practice up to public scrutiny. This is crucial if companies wish to be seen as having a sustainable approach to environmental and social issues.

Legality and Due Diligence

Many of the companies who responded to the questionnaire suggested that the baseline of their procurement requirements was that a legality certificate issued by the Sarawak State Government be in place. Yet the conditions in Sarawak are such that logging operations considered appropriate for state issued legality certificates are environmentally destructive to a degree that would be unacceptable domestically in most importing countries, including Japan, and actively threaten the livelihoods and human/ land rights of indigenous people. This was detailed in our last report *Forest to Floor: How Japan's Housing Construction is Driving Forest Destruction and the Dispossession of Indigenous People in Sarawak*, and has been documented in numerous reports from other groups. This point was a major contributing consideration for the Norwegian government pension fund when they divested from several of the major logging companies in Sarawak in 2010 - 2012. Further, a new report "*Illegal Logging and Related Trade. The Response in Malaysia*" published by Chatham House in January 2015 shows that there has been limited progress since 2010 on tackling illegal logging and trade in such products.¹¹

The European Union has been attempting to negotiate a Voluntary Partnership Agreement (VPA) with Malaysia which would green light the trade of Malaysian

timber in the EU. The EU has far more stringent regulations in regards to the import of timber products than does Japan. The European Commission's 'European Union Timber Regulations' (EUTR) which are legally binding to all member states, provide:

"Timber Regulation counters the trade in illegally harvested timber and timber products through three key obligations:

1. It prohibits the placing on the EU market for the first time of illegally harvested timber and products derived from such timber;
2. It requires EU traders who place timber products on the EU market for the first time to exercise 'due diligence';¹²

Once on the market, the timber and timber products may be sold on and/or transformed before they reach the final consumer. To facilitate the traceability of timber products economic operators in this part of the supply chain (referred to in the regulation as traders) have an obligation to

3. keep records of their suppliers and customers.¹³

However, the VPA, which was initiated in 2006 has stalled due to a number of issues. Most important is that the Sarawak State and Sarawak's timber industry, represented by the Sarawak Timber Association (STA) has stood in opposition to its establishment. The STA published a lengthy defence of its opposition to the VPA in 2009 titled 'MYTH, FACTS & REALITY OF EU FLEGT VPA: SARAWAK'S PERSPECTIVE' which outlines a number of their concerns. These include the concern that strengthened legality requirements would place an economic burden on the harvesting of timber and a general resistance to granting strengthened indigenous land rights. It states that "broader objectives of poverty reduction, growth and sustainable development must be separated from the licensing scheme as they cloud the original intent of the Action Plan to curb illegal logging and associated trade", explaining that "These broader objectives are not only multi-faceted, but complicated and will be better addressed through other avenues".¹⁴

This resistance is symptomatic of the broader issues in relation to logging in Sarawak, namely the timber industry's track record of environmental destruction, human and land-rights violations, poor legal compliance and resistance to change. This approach from Sarawak's loggers exemplifies the point that Sarawak legality certificates are insufficient to prove even the most basic legal requirements that have been established as norms by the international community.

That the Sarawak state government and logging industry will limit its access to European markets rather than change their practices is in part owing to the lax approach of Japan and the willingness of Japanese companies to accept timber products that are tainted by environmental destruction and human rights violations. To be clear, Japan's lenience on illegal wood creates a large loophole globally that undermines the efforts of other countries by providing a market for wood deemed unacceptable elsewhere.

Satisfying legality requirements is not sufficient to ensure that timber products have been produced in an environmentally and socially sustainable way. Japanese companies who purport to have concerns for the environment and a commitment to good practice, must acknowledge that although legality is a threshold requirement, it is a basic bottom line that alone is insufficient to ensure environmentally responsible practice, and in the case of Sarawak, insufficient to ensure that indigenous land rights violations and environmental infractions have not occurred. Four companies were explicit that a legality certificate issued by Sarawak alone was sufficient to meet their legality requirements. These are Noda, Wood One, Asahi Kasei Homes, and Tokyu Land Corporation.

Companies in Japan are already aware of consumer demand that they assure themselves and their customers that their products have not caused unacceptable damage to the environment or human rights. It is a fact of business in the 21st century that a company ethic of achieving high sustainability standards can be positive for brand image and market advantage. Many housing companies claim eco-credentials for their products, but this claim obviously cannot extend to the timber they use.

Japanese companies should take special care to ensure that the timber products that they are procuring are not certified legal by unacceptable legality certificates, and that they adopt a genuine and effective approach to environmental and social sustainability. It is important that such policies actually be implemented and efforts made to ensure that other companies in the supply chain are aware of, and act upon these requirements. In this instance, **it is clear that none of these conditions are currently achievable in relation to Sarawak. The only option is to cease procurement of timber products from that state until it can be assured that these concerns have been addressed. Failure of companies to do so represents a failure to take the aforementioned issues of environmental destruction, indigenous land rights violations and corruption seriously, which will reflect negatively on that company's public image.**

The Problem With Reliance On Certification

Many of the more progressive Japanese companies have expressed a reliance on forest certification schemes to determine and prove the suitability of the timber products they procure, however it is important to note that none of the companies procure only certified timber, they merely claim to preference it. Whilst certification is a step forward, it also poses numerous issues. Many of the companies who said they preference certified timber do not differentiate between certification schemes although such schemes vary significantly, as does their effectiveness. Those companies that do recognise the difference between schemes don't mandate making such a distinction in relation to Sarawak.

Of the international schemes cited, Forest Stewardship Council (FSC) and Programme for Endorsement of Forest Certification (PEFC) are the most common. PEFC provides an umbrella under which local and regional schemes from around the world may be registered. Some companies suggested that they preference FSC over PEFC in relation to Sarawak, however as there are currently no logging operations in natural forests certified by FSC in Sarawak this claim is clearly problematic. While FSC is the superior certification, it still falls short in relation to a number of broader environmental concerns.

The environment movement internationally preferences FSC but it should be noted that no certification scheme guarantees the retention of environmental values across the landscape. This has been an issue of contention within FSC internationally that environment groups are pushing to have addressed via the recognition of the importance of maintaining intact forest landscapes and introducing measures to do so.

PEFC has drawn broad criticism from environment and human rights groups internationally. Claims that it is manifestly inadequate and falls short of providing reliable assurances of sustainability are supported by numerous studies and reports, some of which show that it is incapable of even providing assurances of legality. Greenpeace state:

"PEFC suffers from systemic problems that hide and obfuscate bad practices. The standards are vague and therefore weak, as they can be interpreted as desired by those with bad practices. Governance is controlled by and for the industry, with only token participation by other stakeholders and, audits and the dispute resolution system are likewise controlled by the very actors whose claims of sustainability they are supposed to verify. In other words, the PEFC and its endorsed systems were created to protect an entrenched logging industry."¹⁵

The Malaysian Timber Certification Scheme (MTCS) is the PEFC approved certification scheme most widely used in Sarawak. The MTCS has been found on numerous occasions to be inadequate to even detect illegally logged timber, let alone provide any reliable assurance of sustainability.¹⁶ However, the situation in Sarawak is so extreme, that even the lax guidelines of the MTCS prove to be too challenging for the timber industry, who via their peak body the Sarawak Timber Association (STA) complained that conditions set by Malaysian Timber Certification Scheme for export of timber were a big constraint to the development of the timber industry in the state. They issued a statement saying "At this point, the obvious difference is that our imminent and meaningful objective is to achieve market recognition of our sustainable forest management through the effort of FMC (Forest Management Certification). PEFC on the other hand emphasise on environment and social principles above economic viability"¹⁷ In other words, the situation in Sarawak is so bad, that even the internationally criticised, ineffective and lax regulations promoted by the PEFC scheme have proved too stringent for even the best logging operations in that state to comply with. Sarawak timber interests complain that profits would be adversely affected by the application of environmental and social principles as required for certification, thus relegating ethical production to being an impediment to money-making.

The MTCS has also come under criticism from indigenous groups in Malaysia, with the Indigenous Peoples Network of Malaysia (JOAS) issuing a statement saying "free and prior informed consent is not properly integrated into the MTCS guidelines and not correctly implemented in practice."¹⁸ This should stand as a clear indicator that those Japanese companies who are claiming green credentials, or suggest that they are attempting to influence Sarawak logging companies while waiting for conditions in Sarawak to improve, cannot depend on the industry to regulate itself in an internationally acceptable manner and should immediately cease the procurement of timber from Sarawak.

While in some instances, certification can provide assurances that logging operations are less damaging than they otherwise would have been, this is only in relation to some certifications (FSC) and does not mitigate the fact that many of these areas will be irreversibly compromised regardless of better logging practise. Often certified logging operations in sensitive areas provide a gateway for further destructive activities which will permanently degrade landscapes, and give a false sense of environmental responsibility when the introduction of logging in any form is actually problematic. The concept that significant forest landscapes should remain intact is not yet in practice by any certifiers. Sciencemag found that:

"The certification of logging concessions under responsible management had a negligible impact on slowing Intact Forest Landscapes (IFL) fragmentation in the Congo Basin. Fragmentation of IFLs by logging and establishment of roads and other infrastructure initiates a cascade of changes that lead to landscape transformation and loss of conservation values. Given that only 12% of the global IFL area is protected, our results illustrate the need for planning and investment in carbon sequestration and biodiversity conservation efforts that target the most valuable remaining forests".¹⁹

Certification of logging operations in biodiversity rich, yet sensitive landscapes such as Sarawak can never provide the assurances of sustainability and environmentally responsible practices required. The only way to mitigate the risk posed to these areas is to cease procurement of the products which lead to their destruction. None of the Japanese companies surveyed were prepared to acknowledge this.



Reliance on Japan's New Clean Wood Act²⁰

Several companies explicitly mentioned that they are awaiting the development and implementation of regulations under Japan's new Clean Wood Act of 2016 before changing their policy. This new law has proven to be a major disappointment. Officially named the "Law Concerning the Promotion of Distribution and Use of Legally-Harvested Timber, etc"²¹, it was adopted on 20th May 2016. It will come into force a year later in May 2017 after a Ministerial order fleshing out the application of the law has been developed.

This new law is to complement the ineffectual Green Purchasing Law, known as the *Goho-wood* (legal wood) system. However, the Clean Wood Act also is markedly deficient compared to prohibitions on trading in illegally logged wood product that are in place elsewhere in developed countries, specifically the US Lacey Act, EU Timber Regulation, and Australian Illegal Logging Prohibition Act, if an improvement on Japan's earlier legislation.

The Clean Wood Act is based on voluntary registration only. This is the fundamental flaw. There is no prohibition in the law on importing timber that has been harvested or traded illegally, and therefore no serious penalties for doing so. Neither is there a legal requirement to carry out due diligence. Instead, companies are only expected to make an effort to use legal timber. If they decide to do so, they then register under the new law. The most significant difference from the document-based *Goho-wood* system is that businesses wishing to register will then have to carry out some form of due diligence.

Several key elements are to be determined by May 2017, including; (1) Due diligence system standards; (2) the legality definition; (3) how to ensure that businesses register under the voluntary system, particularly those dealing in high-risk timber; and (4) how to monitor and regulate non-registered companies.²²

It is currently unknown what the Japanese due diligence system will entail, except that it contains the following four elements; (1) risk assessment; (2) risk mitigation; (3) requirements for traders; and (4) records management.²³

An incentive for carrying out due diligence is that companies are only allowed to call themselves "registered operators in timber related business" if they have enrolled in the system. Non-registered companies will be subject to penalties if they use this term.

The definition of legal wood is also yet to be clarified. Legal timber is defined in Article 2 as "wood derived from trees logged in compliance with laws and

regulations of Japan or the country of origin." Those familiar with the situation in Sarawak will be aware that such a definition can encompass wood of dubious origin. Further passages in the law imply that elements of social issues and sustainable forest management should be taken into consideration, although how that would occur and whether such measures would be satisfactory is not yet known.

The new law covers most wood and timber products, including products with more complex supply chains such as paper and furniture. Operators covered by the law include most businesses dealing in timber and timber products – whether manufacturing, processing, importing, exporting, or sale (except at a retail level). The construction industry using timber is included. It is thought that businesses importing high risk products will become focus industries for registration, although this will become apparent when the Ministerial order is issued.

Enforcement measures are designed to mostly focus on issuing administrative orders for remedial actions (such as withdrawal of registration status, request for information disclosure and inspections). Relevant Ministers have the power to ask for reports or carry out unannounced inspections both for operators and for registering organisations. There will be no monetary penalties for dealing in illegal wood.

We understand that industries importing wood and utilising wood from overseas are currently lobbying for minimal standards. The Sarawak Timber Association (STA) has also been lobbying in Japan for the continuance of the trade without the constraints that effective legislation would deliver.

Sarawak Specific Matters

1. Indigenous rights to forests

Logging in Sarawak has a negative impact on Indigenous people who rely on Sarawak's forests for sustenance, shelter, cultural maintenance and their livelihoods. There are over one million Indigenous people living in Sarawak. The Malaysian federal state recognises Indigenous peoples' native customary rights (NCR), however the Sarawak government has failed to enshrine these rights in its Land Code.²⁴ Timber concessions are often awarded on land that is claimed by Indigenous people.²⁵ Government interference with local Indigenous councils has pressured already persecuted Indigenous groups into conceding more forest to logging. These issues have been investigated by the Malaysian Human Rights Commission (SUHAKAM), who made a number of recommendations including

in relation to administration and remediation of alienation of NCR land, but it is reported that the Sarawak government has failed to act.²⁶

Indigenous people of Sarawak have resisted the logging companies with protests, legal actions and international outreach campaigns for decades. Often these acts of resistance from the Indigenous peoples are met with police violence. Hundreds of cases contesting the government's allocation of ancestral lands for the purposes of logging and plantations have come before the court. Indigenous people have consistently attempted to challenge logging companies and the government on their abuse of NCR land. In the minority of cases when there have been favourable findings in a judicial system which is not responsive to traditional Indigenous rights and interests, the judgements have not been acted upon by government and therefore the degradation of ancestral lands has continued.²⁷



In December 2016, the Malaysian federal court ruled against Dayak people in Sarawak who were claiming NCR status over their ancestral forest lands. The court ruling found, with one judge dissenting, that indigenous people had no claim over the virgin communal forests that sustained their livelihoods and culture, that the Native Customary Rights (NCR) of the indigenous Dayak people apply only to a limited area of farmland and not to the forest areas around their traditional longhouses. The Dayaks say they have customary rights over the "territorial domain" around their longhouses, including primary forest within that domain, which is usually owned by the community.

The ruling was a devastating blow to the indigenous people of Sarawak, and is expected to affect over a hundred claims throughout the state.²⁸ The final hope is now for a review of the decision by a different panel of judges. A legal issue still needs to be resolved, because there is a contradiction in the judgement. This contradiction is about the application of the 'common law', a form of customary law applied in Commonwealth jurisdictions, including Malaysia. Authorities from other Commonwealth countries say that the customs of indigenous people are under the common law rather than being under the statutes or laws of a country. Yet the majority of judges in this case in Malaysia relied on the fact that no statute or law of the country exists that recognised the rights that were disputed. The claim is that the common law is the alternative and equally valid law that applies in these circumstances.

2. Corruption

Corruption in the allocation of logging concessions and the oversight of the conduct of logging and processing operations is endemic in Sarawak and has been widely reported for years. In his book "Money Logging – On the trail of the Asian Timber Mafia" Lukas Straumann investigated and documented the network of criminals who have earned billions through illegal timber sales and corruption.²⁹ He identifies Abdul Taib Mahmud, former governor of Sarawak, as the kingpin of this timber mafia. He shows that Taib's family have profited by around \$US 15 billion, laundering and secreting the money overseas. Taib is now under investigation by the Malaysian Anti-Corruption Commission.

The International Corruption Perceptions Index (CPI)³⁰ published by Transparency International generally takes a broad nationally focussed approach to identifying corruption that in the past has not brought the corruption in Sarawak into focus because Peninsula Malaysia had much better governance. However, Malaysia moved into a high risk rating on corruption on January 25 this year. Companies should take this seriously.

When governor Adenan succeeded Taib as Chief Minister in Sarawak in 2014 he acknowledged the problems of corruption in the timber industry and signalled a major crackdown. This largely tackled small and medium sized companies but did not focus on the Big 6 logging companies, likely to be the main culprits, that are responsible for most logging and who are politically well connected. These companies were reported to have made major contributions to the election campaign that returned his government in 2016. Following the passing of Adenan in January 2017, his successor Abang Johari is expected to continue in a similar manner. He has announced a change to governance which provides that short term timber licences will now be awarded via a transparent tender process. These will be issued only for state forest land which has been approved for development and Native Customary Land (NCL) Development Area and Native Communal Reserve that shall undergo development³¹. This is an improvement in governance, but does not resolve the larger issues around forest devastation and the impacts on human rights of indigenous people.

Appraisal

Despite decades of campaigning and worsening conditions in Sarawak, Japanese companies still remain unwilling to take steps to ensure the products that they use are not contributing to the ongoing human rights abuses, environmental destruction, corruption and illegality that plague the Sarawak timber industry. With only a few minor exceptions, Japanese housing and condominium construction companies remain without effective policies in relation to sustainability, human rights and even legality. Such measures have generally been put in place amongst companies in other developed economies.

While Japanese companies lag far behind the rest of the world, eNGOs (including Markets For Change) have campaigned for decades to encourage companies to take responsibility for the products that they are utilising. The 2016 report of Markets For Change and JATAN: *Forest to Floor, How Japan's Housing Construction is Driving Forest Destruction and the Dispossession of Indigenous People in Sarawak* established that Sarawak timber products were prevalent throughout the Japanese supply chain. We conducted numerous meetings and seminars in Tokyo and Osaka with Japanese housing and condominium construction companies as well as large trading houses and flooring manufacturers, informing them of the issues. We outlined that the meagre five percent of remaining intact natural forest could not withstand the ongoing environmental degradation in Sarawak. The timber industry was creating an irreversible situation that was pushing many species to the brink of extinction while destroying more and more natural forest. Natural regeneration of degraded forests was not practiced. Instead these forests were repeatedly

cut over and eventually converted to plantations. Natural values and traditional indigenous homelands and lifestyles are irretrievably destroyed.

Even the most progressive of housing and condominium construction companies in Japan didn't have appropriate procurement policies in relation to Sarawak. They do not differentiate Sarawak as an extreme case in relation to environmental and human rights impacts and the rule of law. Instead they rely on a slow, sliding scale progression in relation to procuring Sarawak products, preferring to rely on the hope that the situation would resolve itself rather than apply serious pressure on suppliers. Few companies seek alternative, less destructive timber supplies outside of Sarawak, as we consistently recommend. Whilst a few may be increasing domestic timber supply for flooring, this is not to the point of excluding Sarawak sourced timber and making a complete substitution with low risk sources. Yet that is the action required to be taken by any company wishing to be properly responsible in its procurement. In effect, even the most aware companies had an approach which can be characterised as *too little, too late*.

Japanese companies have repeatedly implied that they were depending on new legislation passing the Japanese parliament to determine the conditions of sustainability and legality in relation to the timber products they procure. The new legislation has proven to be woefully inadequate, because it does not make it illegal to trade in illegal wood products. Under the new law, the evaluation of timber sources by each company is key, so if the new law is to work effectively participating companies would identify Sarawak as a high risk area for environment and human rights even if they get some formal proof or paper from the Sarawak government. Thus they would exclude Sarawak sourced material. It is not necessary to await the implementation of the new law before taking this vital decision. It is clear that if Japanese companies have any concern for Sarawak's people and forests, they must take it upon themselves to act responsibly and immediately cease procuring timber products from Sarawak. Failure to do so will result in the inevitable complete destruction of Sarawak's intact natural forests and be the final blow to many species on the edge of extinction.

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