

COUNCIL ON ETHICS

THE GOVERNMENT PENSION FUND GLOBAL

To the Ministry of Finance

Recommendation of 15 September 2010

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1 Introduction

The Council on Ethics has assessed whether the Malaysian company Lingui Developments Berhad's forest operations in Sarawak, Malaysia, cause severe environmental damage.¹

Lingui Developments Berhad² is a listed Malaysian integrated forest and wood-products company. Its operations include logging and forest management of natural forest in Malaysia as well as palm oil plantations.³ As of 2 August 2010 the Norwegian Government Pension Fund Global held 1,584,100 shares in the company.

Lingui is a subsidiary of Samling Global Limited, and Samling has a 67.23 per cent share in the company.⁴ On 22 February 2010 the Council on Ethics submitted a recommendation to exclude Samling Global⁵ from the Government Pension Fund on the grounds that the company's illegal logging may cause severe environmental damage.

The Ministry of Finance published the Council's recommendation on 23 August 2010 after the Fund had divested from the company. The recommendation was mainly based on the Council's own investigations of Samling's forest operations in Sarawak (Malaysia) and Guyana. The investigations documented what appeared to be extensive and repeated breaches of the licence requirements, regulations and other directives in all of the six concession areas that were examined in Sarawak. Some of the violations were very serious transgressions, such as logging outside the concession area, logging in a protected area that was excluded from the concession by the authorities in order to be integrated into an existing national park, and re-entry logging without Environmental Impact Assessments.

Two of the concessions which were examined belong to wholly-owned subsidiaries of Lingui. In a third concession, a further Lingui subsidiary carries out the logging operations for another of Samling's tier-subsiidiaries. Thus the Council considers Lingui to be equally responsible for the illegal logging and severe environmental damage which were disclosed in these concessions. The Council wrote a letter to Lingui on 25 August 2010, giving the company an opportunity to comment on the Council's draft recommendation. Lingui has not responded to the Council's letter.

The Council recommends the exclusion of Lingui Developments Berhad from the investment universe of the Government Pension Fund Global due to an unacceptable risk of the company contributing to ongoing and future severe environmental damage.

2 Background

Lingui's parent company, Samling Global Ltd, is an integrated forest and wood products company with forest resources, processing facilities and distribution networks in Guyana, New Zealand and China. Samling has 15 selective timber logging licences in Sarawak, Malaysia, covering an area of approximately 1.4 million hectares of natural rainforest.

¹ According to the Guidelines for Observation and Exclusion from the Government Pension Fund Global's Investment universe, Section 2, paragraph 3, letter C.

² Hereafter also referred to as Lingui.

³ <http://www.lingui.com.my/home.html>

⁴ <http://www.samling.com/eng/aboutus/group.htm>

⁵ Hereafter also referred to as Samling.

Samling's timber harvesting operations appear to be organized through its subsidiaries Barama Company Limited, Syarikat Samling Timber Sdn. Bhd. og Lingui Developments Berhad. The two first-mentioned are wholly owned subsidiaries of Samling, while Samling holds a 67.23 per cent share in Lingui.⁶ Lingui is listed on the Malaysian stock exchange. The forest concessions are owned and managed by wholly owned subsidiaries of Samling Global's subsidiaries.

The Council on Ethics' recommendation on the exclusion of Samling Global shows that Lingui Developments is directly involved in three of Samling's concessions in Sarawak that were examined by the Council. A short summary of the Council's findings is provided below.⁷

Concession T/0294 – Ravenscourt Sdn. Bhd.

The timber licence belongs to Ravenscourt Sdn. Bhd, a wholly-owned tier-subsiary of Samling Global. The logging operations, however, are carried out by Tamex Timber Sdn Bhd , a subsidiary of Lingui. Tamex Timber is acting as a contractor for Ravenscourt Sdn. Bhd.

Extensive and intensive logging has been conducted under this license from May 2007 to May 2009 in an ecological core area around the Batu Lawi Mountain, north of the existing *Pulong Tau National Park*. In May 2008 the Sarawak forest authorities excluded this particular area from the timber licence, meant to be included in the existing national park. Satellite imagery reveals that the logging has been carried out more than one year after Ravenscourt was duly informed by the authorities that the area in question would be excluded from the concession, and that logging should be stopped.⁸

Analyses using terrain data from Google Earth indicate that some of the areas currently being logged are so steep (in excess of 35 degrees), that conventional land-based logging normally is not permitted.⁹ One particular area of very intense logging extends about 300 m up the mountain's eastern side. Illegal logging in steep terrain also occurs in another part of the concession, Coupe 05A, where a large swathe of steep terrain adjoins the border with the existing national park. A logging road has recently been cut for a distance of approximately 3 kilometres into the Class IV terrain zone.¹⁰ Intensive logging activity has been carried out here, and extensive erosion was observed.

Concession T/0411 - Samling Plywood (Baramas) Sdn. Bhd

The licensee in this concession is Samling Plywood (Baramas) Sdn Bhd, a wholly owned subsidiary of Lingui, while the logging is being carried out under contract by Samling Global's subsidiary Syarikat Samling Timber Sdn Bhd.

The Council's research indicated that Samling has performed re-entry logging in T0411 for more than three years without the Environmental Impact Assessment (EIA) required by *the Natural Resources and Environment (Amendment) Ordinance* of 2005.¹¹ Furthermore, satellite images

⁶ <http://www.samling.com/eng/aboutus/group.htm>

⁷ See the Council on Ethics' recommendation on Samling Global for a comprehensive account of the circumstances.

⁸ Letter from the Sarawak Director of Forests to Ravenscourt Sdn, Bhd dated 13 May 2008 regarding the extension of Pulong Tau National Park in areas within Licence No T/0294. The letter is appended to the EIA for re-entry logging in T/0294, both on file with the Council. Approved concession maps and Permits to enter Coupe show the exact boundaries of the area of the licence involved. The map for Coupe 14A, which includes the Batu Lawi-massif, clearly shows that the area is to be preserved, and that no logging must be carried out here.

⁹ The so-called Class IV terrain areas refer to slopes in excess of 35 degrees. In general, conventional land-based logging and road construction are not permitted in these areas.

¹⁰ See footnote 9.

¹¹ The Natural Resources and Environment (Prescribed Activities) (Amendment) Order, 1997, First Schedule, Article 2 (i); see also table 2.

reveal ongoing logging and extensive road construction in two areas within the concession's Coupe 4A. These areas are classified as Class IV steep terrain in maps of the licence area and in permits to enter coupes.¹² In Class IV areas, only helicopter logging is permitted. As of January 2009 permission had yet to be granted for the company to begin logging operations in two blocks (75H-78H). All the available information therefore suggests that the land-based logging and road construction in this area are illegal.

Completely clear-cut forest on both sides of the road for distances of up to 50 metres or more, including the removal of undersized trees was observed during the field investigation. Also the forest within river buffers had been cleared in large areas, and logging debris was seen clogging rivers and streams throughout the area. Such logging practises appear to be in violation of the official standard regulations, which normally impose stricter requirements for logging along roads and rivers than what was seen in this area.

Concession T/0413 - Samling Plywood (Miri) Sdn. Bhd.

Concession T/0413 belongs to Samling Plywood (Miri) Sdn. Bhd. which is a wholly owned subsidiary of Lingui.

In this concession, an area that had been logged in 2003-2004 was selected for field investigation. In the area, which was visited during the field investigation, stumps on the bank of the river (the Semariang river) indicated cutting within the buffer zone, including cutting of protected tree species (Engkabang trees¹³) and logging of undersized trees. Logging debris had not been removed from the river. A hidden log pond was found, which according to local residents was used for storing illegally logged timber (protected tree species and undersized trees). Local villagers asserted that these findings were not isolated cases, reporting that the company had cut trees along the river for several kilometres, and that numerous Engkabang trees had been logged in the area.¹⁴

3 The Council on Ethic's letter to Lingui

In accordance with the Ethical Guidelines point 5.3, the Council wrote a letter to Lingui, dated 25 August 2010, providing it with the opportunity to comment on the recommendation. The company has not responded to the Council's letter.

4 The Council's assessment

Illegal logging refers to the harvesting, transporting, selling or buying of timber in contravention of national law. According to the preparatory work for the Ethical Guidelines, illegal logging may be in breach of the Ethical Guidelines.

In its assessment of Samling, the Council emphasised the extent of illegal logging in Samling's concession areas, whether the violations appeared to be systematic, and the probability that the

¹² This area covers logging blocks 75H, 76H, 77H and 78H, and also 68H. On-site investigations in April 2009, analysis of GPS readings, and comparison with satellite imagery and concession maps and Permits to Enter Coupe

¹³ The Wildlife Protection Ordinance lists 7 species of Engkabang (also known as Meranti): *Shorea splendida*, *Shorea helmsleyana*, *Shorea siminis*, *Shorea pinanga*, *Shorea macrophylla*, and *Shorea stenoptera*. The last three are listed on the International Union for Conservation of Nature's (IUCN) red list of threatened species, classified respectively as vulnerable, endangered and critically endangered.

¹⁴ Interviews with villagers from Long Makaba conducted during the field investigation in September 2009.

company's behaviour will continue in the future. The Council also stressed that illegal logging, particularly in natural forests, often results in far-reaching and lasting damage to the forest and the environment. Finally, the Council highlighted the comprehensive international and national efforts to combat illegal logging in Asia and elsewhere, under the auspices of the EU, the World Bank and individual States, including Norway.¹⁵ In this context, the Norwegian and international initiatives aimed at preventing deforestation and forest degradation in tropical rainforests as part of the work to reduce emission of greenhouse gases and loss of biological diversity are also relevant.¹⁶

In the recommendation on Samling, the Council's investigation of the company's forestry operations in Sarawak documented extensive and repeated breaches of licence terms, regulations and other requirements in all the six concession areas that were surveyed. The Council found some of the violations to be very serious, such as logging in a protected area that had been officially excluded from the concession in order to be integrated into an existing national park, and re-entry logging without Environmental Impact Assessments. These offences occurred in concessions where Lingui is the licensee or is conducting logging operations on behalf of the parent company. Other practices which, seen in isolation, appeared to be less serious are aggravated because they seemed to be a systematic part of Samling's forestry operations. In the concessions investigated, clear-cutting had been carried out along the roads across wider sections than what is permitted, clear-cutting had occurred in riparian buffer zones, and rivers and streams were polluted by logging debris; roads had also been built and conventional logging taken place in areas of steep terrain where only helicopter logging is allowed. Furthermore, instances of logging of protected species and of undersized diameter trees were detected. Such practices were also revealed in the concessions where Lingui is involved. Lingui's operations, therefore, do not appear to be any different from how forest operations are carried out in the other Samling concessions.

Samling commented on the Council's draft recommendation on the exclusion of the company. In its comments, Samling raised doubts about the Council's methods and sources, but failed to provide any specific information or documentation that illuminated or countered the basis for the Council's recommendation. Regarding the concessions where Lingui is involved, Samling did not comment either on the logging in the protected area, the cutting of protected tree species or the logging of undersized trees. Samling acknowledged one instance of illegal logging and road construction in steep terrain without specifying where this has occurred, whereas with regard to the other irregularities that have come to light, it denied any wrongdoing without substantiating this with documentation. Thus, the Council found that Samling's reply did not provide grounds for altering the Council's conclusion that the company is involved in illegal logging.

The Council considers that Lingui, as licensee and logging contractor for the parent company, Samling Global, is directly involved in the illegal logging and severe environmental damage which has been disclosed through the Council's investigations of Samling Global's forest operations in Sarawak. The Council on Ethics therefore recommends the exclusion of Lingui from the Fund.

¹⁵ Such initiatives include the EU Forest Law Enforcement, Governance and Trade (FLEGT), and regional FLEG processes supported by the World Bank and the Asia Forests Partnership (AFP), as well as numerous national initiatives aimed at halting the trade of illegal timber and wood products. Malaysia is partner to both EU Flegt and AFP. See for example <http://ec.europa.eu/environment/forests/flegt.htm> and <http://www.asiaforests.org/>.

¹⁶ See for example the Norwegian Government's Climate and Forests project, <http://www.regjeringen.no/nb/dep/md/tema/klima/klimaogskogprosjektet.html?id=548491>.

5 Recommendation

The Council recommends the exclusion of Lingui Developments Berhad from the investment universe of the Government Pension Fund Global due to an unacceptable risk of contributing to current and future severe environmental damage.

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