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**FOOD AND AGRICULTURE
ORGANIZATION OF THE
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Proceedings

Joint UNECE/FAO Roundtable

Trade, Environment and Forests - Working Together for Sustainable Development

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Roundtable Focal Points

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Introduction

Background

The need to obtain synergies between trade and environment policies is recognised as one of the most urgent, sensitive and complex policy questions of the day. The forest and forest products sector exemplifies many of these issues, as

- forests are vital to the environment,
- there is a very significant trade in forest products,
- there are many externalities and market distorting features arising notably from the multiple functions of forests,
- there are some innovative developments, notably the certification of that products entering international trade come from sustainably managed forest, and
- there is a broad public interest in sustainable forest management and conservation as well as an intense international dialogue on forests.

The ongoing multi-polar discussions relevant to sustainable forestry development and to trade call for exchanges of ideas and information between the various policy communities. Together, FAO and UNECE have therefore taken the initiative to organise an open-ended roundtable on trade and sustainable forest management in order to facilitate the exchange of views between the different constituencies with an interest in the issue of trade and sustainable forestry development.

This roundtable is based on ongoing work in the organisations:

- The FAO Forest Products Division has carried out extended research and analysis on various trade-related issues impacting on the forestry sector and interlinking forest products trade and forest management is through its regular programme. Additionally, FAO is currently implementing a project entitled *Impact Assessment of Forest Products Trade in the Promotion of Sustainable Forest Management* financed by the Government of Japan.
- UNECE has organised several special topic discussions at the Timber Committee aiming to bring together representatives of trade and environment sectors as well as forest sector specialists. It also monitors markets for certified forest products on a continuing basis, in the context of its continuing monitoring and analysis of forest products markets and trade.
- The FAO Liaison Office in Geneva has held a series of roundtable briefings for WTO delegations from developing countries on a wide range of topics.

Objective

The objective of this Roundtable is to engage trade policy makers and trade negotiators at the international level, particularly those in WTO negotiations, in exchanging information and views on outcomes and key issues of the current discussion process on trade and sustainable forest management in order to enhance the potential of trade for sustainable forest management.

Key Issues and Key-Note Speakers

Recent Trends and Policy Development

- (i) Trade Liberalisation and Forest Products Trade – David Brooks, US Trade Representation
- (ii) Forest-related Multilateral Environmental Agreements (MEAs) and Current Policy Debates in WTO – Rupert Schlegelmilch, European Commission
- (iii) Forest and Forest Products Certification - NN Malaysia

Impacts of Trade in Forest Products and Services

- (i) Trade, Rural Poverty and the Environment - Owen Cylke, WWF US
- (ii) Markets for Forest Environmental Services – Markku Simula, INDUFOR Finland
- (iii) Private Sector Perspectives on Developments of Trade in Forest Products and Services – Ivan Tomaselli, STCP Brazil

Expected Results

Based on the presentation of key issues, the Roundtable should provide a neutral forum for discussion on obstacles and limitations, potentials and steps to be taken to achieve the overall objective to encourage sustainable forest management. The Roundtable is expected to constitute an opportunity for trade policy makers and trade negotiators to address the concerns of the forestry community that trade liberalization processes are unaware of the certain imperatives for sustainable forest management, both for producer and consumer countries alike.

Conduct of the Roundtable

The Roundtable will be chaired by a FAO staff member inviting a key note speaker to address key issues of concern and moderating the discussion during the following sessions. The one-day meeting is organized to serve as a neutral forum, in an informal set-up, for an open exchange of views and policy positions and participants are invited in their personal capacity.

Invitees

The Roundtable is intended to bring together some 100 trade policy makers and trade negotiators from governments and inter-governmental organizations like WTO, UNCTAD and others, along with forest sector experts.

Collaboration

The Roundtable is organized by the FAO Forest Products Division (FOP), the FAO Liaison Office in Geneva and the United Nations Economic Commission for Europe (UNECE).

Date and Venue

The Roundtable will take place in Geneva at the Palais des Nations, Salle V, on 9 July 2003 from 10.00 –13.00 and 14.30-17.30. There will be simultaneous interpretation in English, French, Russian and Spanish. The Roundtable will be held adjacent to the Regular and Special Sessions of the Committee on Trade and Environment (CTE) of the World Trade Organization (WTO).

2. Provisional Agenda

A.M. Session - 9.30 – 12.30

Opening Session

9:30 Opening Remarks – T. Masuku, Director,
FAO Liaison Office in Geneva

Opening Address by the Chair – W. Killmann, Director,
Forest Products and Economics Division, FAO, Rome

Overview – C. Cosgrove-Sacks, Director,
UNECE Trade Development and Timber Division

Session I – Recent trends and policy development

10:00 Trade Liberalisation and Forest Products Trade - David Brooks,
Office of the US Trade Representative

11:00 Forest-related Multilateral Environmental Agreements (MEAs) and Current
Policy Debates -Rupert Schlegelmilch, European Commission

12:00 Forest and Forest Products Certification - Suboh Mohd Yassin, Deputy Secretary
General of the Ministry of Primary Industries Malaysia

P.M. Session 14.30 – 17.45 p.m.

Session II – Impacts of Trade in Forest Products and Services

14:30 Trade, Rural Poverty and the Environment – Owen Cylke, WWF US

15:30 Markets for Forest Environmental Services – Markku Simula, INDUFOR Finland

16:30 Private Sector Perspectives on Developments of Trade in Forest Products and
Services – Ivan Tomaselli, STCP Brazil

17:30 Closing Remarks

Reception (Palais des Nations, 8th Floor Restaurant)

3. Introductory Remarks by Themba N. Masuku

Director, FAO Liaison Office in Geneva

Excellencies, Distinguished Ladies and Gentlemen; Colleagues

Let me take this opportunity to extend to you all a very warm word of welcome to this roundtable on Trade, Environment and Forests. Some of you have by now become familiar with the FAO organized roundtables to inform negotiators and policy-makers on important and relevant topics, such as food security and others. Your coming today gives a clear indication to us that these roundtables have been and are useful, and we are encouraged.

The past roundtables have been a single undertaking by the FAO alone, and this time we have joined with the ECE to conduct this roundtable. Meanwhile, I note that the ECE has, in the past, separately conducted several special topic discussions at the Timber Committee level on relevant issues, and we have found value in conducting a joint roundtable to pursue these topics.

We hope that this roundtable will provide a good forum for the exchange of views, and this way we shall continue to build capacity – especially for those involved in the negotiations at the WTO on environment and other topics.

Excellencies, Ladies and Gentlemen, sustainable development is the key to all that we do in development, and as we look back at the World Summit on Sustainable Development there is no doubt that we need to increase our understanding of the challenges that we face. It is open-ended roundtables like this one that can provide an informal environment to discuss and deepen our understanding on the kinds of issues that we shall be discussing today.

We have lined up speakers to introduce the issues, after which we can all express our views in an interactive manner. Excellencies, Ladies and Gentlemen, I shall stop here and introduce my colleague, Mr Wulf Killmann, who will chair the proceedings.

4. Opening Address by the Chair

Wulf Killmann, Director, Forest Products and Economics Division, FAO

Ladies and Gentlemen, dear Colleagues,

On behalf of the Director-General of the Food and Agriculture Organization (FAO), I would like to welcome you to this Roundtable entitled Trade, Environment and Forests – Working together for Sustainable Development. This event is a joint initiative of the FAO Forest Products and Economics Division in Rome, the UN Economic Commission for Europe (UNECE) and our FAO Liaison Office here in Geneva. I would like to take this opportunity to thank Ms Carol Cosgrove-Sacks of UNECE and Mr Themba Masuku of the FAO Liaison Office and their teams for their effective cooperation and for their opening and closing remarks.

The need to achieve synergies between trade and environment policies is recognised as a sensitive and complex policy question of the day. The forest and forest products sector exemplifies many of the issues at stake, as the multiple functions of forests are vital to the environment and there is - on the other hand - a significant trade in forest products. There are some innovative recent developments, notably the certification of forests and forest products entering international markets, coming from sustainably managed sources. And most importantly, there is a broad public interest in sustainable forest management and conservation as well as an intense international dialogue on forests which has an ever-increasing impact on forest products trade and the emerging markets for environmental services of forests.

Therefore, the objective of this Roundtable is to engage trade policy makers and trade negotiators at the international level, particularly those involved in WTO negotiations, in an exchange of information and views on the key issues of trade policy development and its interaction with policies in support of sustainable forest management.

This roundtable is based on ongoing work in FAO and UNECE, namely:

- FAO has carried out extended research and analysis on various trade-related issues impacting on the forestry sector and interlinking forest products trade and forest management. Additionally, FAO is currently implementing a project entitled *Impact Assessment of Forest Products Trade in the Promotion of Sustainable Forest Management*, financed by the Government of Japan. An international expert consultation on impacts and interactions of trade and sustainable forest management was organised earlier this year in Rome.
- UNECE's Timber Committee has held several discussions aimed at bringing together representatives of trade and environment sectors, as well as forest sector specialists.
- The FAO Liaison Office in Geneva has held a series of roundtable briefings for WTO delegations from developing countries on a wide range of topics.

We are delighted that six colleagues from across the world have agreed to be with us today and to present their views on some key issues which are of greatest importance for the policy debate and cooperation between the trade and the forestry communities. In the morning we shall discuss “Recent Trends and Policy Development”, in the afternoon the Impacts of Trade in Forest Products and Services.

As outlined in the agenda, each presentation will be followed by an open discussion in plenary.

We hope that this Roundtable will be a useful forum for discussion on obstacles and limitations, potentials and steps to be taken to achieve a greater positive impact of trade on the developments in sustainable forest management, and the possible need of increasing the collaboration between trade-related policy processes and the processes on sustainable forest management.

Thank you for your attention.

5. Overview by Carol Cosgrove-Sacks

**Director, Trade Development and Timber Division,
UN Economic Commission for Europe**

- The World Summit on Sustainable Development (WSSD), Johannesburg, September 2002, made the commitment to enhance the mutual supportiveness of trade, environment and development with a view to promoting sustainable development.
- There is increasing interdependence in world trade, especially through international supply chains.
- As Joseph Stiglitz (IMF) says, it is not globalisation itself nor the expansion of world trade which is the problem, as these mega trends are broadly irreversible and generally positive. Rather, it is how globalisation is implemented and the legal, institutional, economic and social measures which accompany it. This is at the heart of the Doha Development agenda. Thus the interrelation between trade and environment and sustainable development is truly one of the major challenges of our age, and one that we must together resolve. I am very happy to have the combined resources of FAO and UNECE to examine these issues today.
- The forest and timber sector is one of the hot spots in the trade/environment discussion, for many reasons:
 - There is an acute global problem – deforestation with all the caravan of economic, social and environmental suffering which it brings in its train.
 - As there is an active global trade in forest products, and many countries suffering from deforestation are also exporters, many activists, experts and governments have enthusiastically promoted trade related measures as one way in which the industrialised countries can influence the trend: this aroused concerns about infringement of sovereignty, and the creation of technical barriers to trade masquerading as environmental protection measures.
- Key Questions:
 - What exactly is “sustainable forest management”?
 - Is sustainable forest management the same everywhere?
 - Who decides what is sustainable and what is not?
 - Is a certification system, as proposed, initially by NGOs, compatible with the rules-based international trade regime as laid down in the GATT/WTO?

- o Does trade in forest products encourage sustainable forest management or the contrary?
 - o How do we ensure that certification requirements do not themselves become new technical barriers to trade?
 - o How to take properly into account in policy and practice the many and widely varying non-market benefits of forests, such as conservation of biological diversity, soil and watershed protection, aesthetic pleasure, carbon sequestration, or recreation?
- I believe that the response by the forest and timber sector as a whole to these complex issues over the last ten or so years has been an example to other sectors. Special features have been:
 - o Intense dialogue in many fora, with many stakeholders, maintained despite strong tensions between certain players;
 - o Respect for national sovereignty and agreed international trade rules
 - o Innovative initiatives, notably certification mechanisms, flexibly applied in a free market context
 - o Acceptance of the complexity of the policy issues and desire to find consensus solutions.
- Today we are hosting an open forum. This is not a formal intergovernmental meeting or a decision-making body: the aim is to promote improved understanding. There will be no formal statement at the end. Participants represent only themselves, so please feel free to express opinions and ask questions in an open manner.

6. Session 1 - Recent Trends and Policy Development

6.1 TRADE LIBERALISATION AND FOREST PRODUCTS TRADE – BY: DAVID BROOKS, OFFICE OF THE US TRADE REPRESENTATIVE



Trade and Forest Management: Trends and Policy Developments

Dr. David J. Brooks
Office of the United States
Trade Representative



Key Messages

- Forest products trade has increased in absolute and relative importance
- Trade has reinforced broad-scale trends in management, production, and consumption
- Further gains from trade liberalization and economic integration are possible
- Continuing need for a framework for standards and protection against forest pests/diseases

Global Context

- Deeper and wider integration supported by trade and investment liberalization
- Expanding and evolving debate over forest management practices
- Increasing recognition of non-commodity value of forests
- High profile resource policy issues with trade links

Market and Industry Trends

- Short-term market disturbances and mixed patterns of economic growth
- Structural change, increasing competition in major markets, and emerging producers
- Consolidation and capacity adjustment
- Increasing importance of direct investment

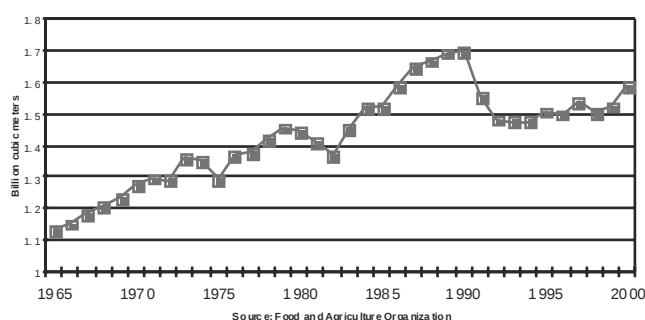
Market and Industry Trends

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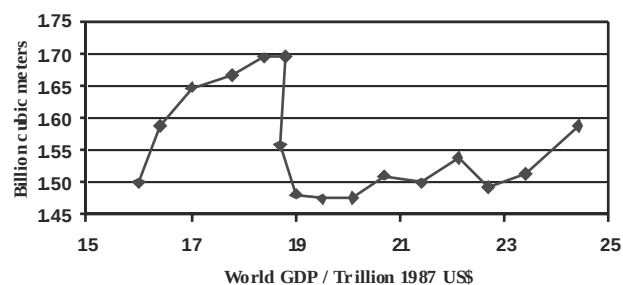
Management Trends

- Greater reliance on managed forests, private forests, plantations, and recovered fiber
- Increasing share of timber produced in managed, including intensively-managed forests
- Increasing importance of investment and management organizations
- Greater effort to market good management

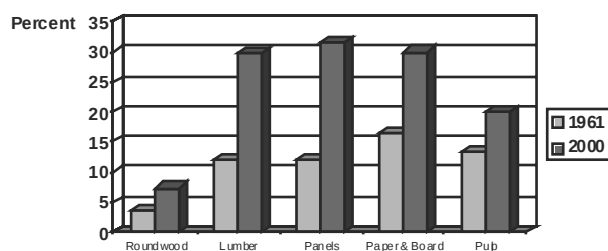
World Production of Industrial Roundwood, 1965-2000



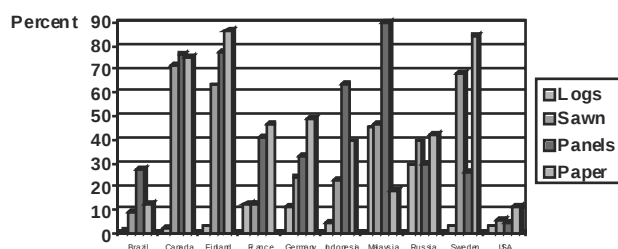
Industrial Roundwood Consumption and World GDP, 1985-2000



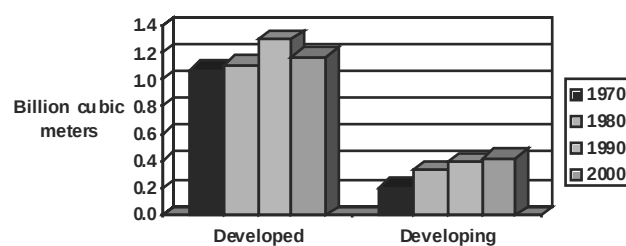
Share of World Production Entering Trade, 1961 and 2000



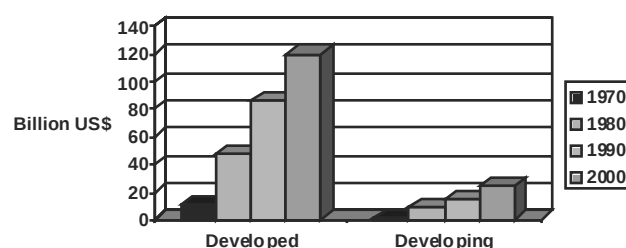
Share of Production Exported, 2000



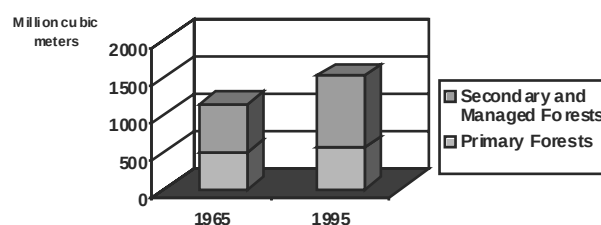
World Timber Production, 1970 to 2000



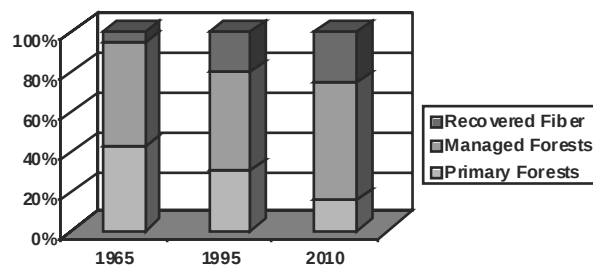
Value of Forest Products Exports, 1970 to 2000



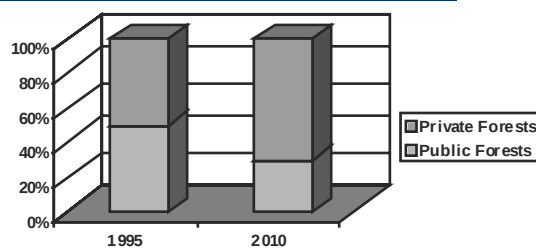
Estimated Sources of Industrial Wood Fiber, 1965 and 1995



Estimated and Projected Sources of Industrial Wood Fiber



Estimated and Projected Sources of Industrial Wood Fiber



Summary Points

- Further trade liberalization can be consistent with both development and improved management of forests
- Some countries will benefit more than others
- The mix of products and location of production will change
- Importance of trade should not be overstated

Summary Points

- Policies other than trade policies are the primary tools for SFM
- Evidence that market barriers (import or export) may undermine rather than support SFM
- Market barriers may shift rather than reduce environmental effects

Summary Points

- Efforts to liberalize should address both tariff and non-tariff barriers
- There is a continuing need for
 - effective protection against forest pests and diseases
 - a framework for standards

Discussion

Based on one of the summary points that the current debate and measures on trade liberalisation should address import/export tariffs and non-tariff barriers alike, it was noted that empirical data show very complex dynamics. There seems to be a tendency, as tariffs decline, for non-tariff barriers to become a relatively more important factor in forest products trade. As a consequence, it was underlined that governance issues should be addressed and institutions strengthened before tariffs are reduced, in order to enable governments to supervise forest management and trade in forest products and to fulfil their normative functions with regard to policies and legislation.

It was also stated that trade liberalisation does not necessarily impact positively on sustainable forest management and sustainable livelihoods, particularly of the poor. However, transparency, information exchange and measures to support informed consent within a given society could probably support effective policy development for sustainable forest management in a much better way than trade policies aiming at trade liberalisation. It was noted that there should be a sound and sustainable balance between information exchange, transparency and focused policy making – other than trade policies - to overcome the usual rhetoric in debates on sustainable forest management.

It was also noted that, besides the “world forest products economy”, domestic markets, which are not subject to international trade rules and trade negotiations, continue to play an important role in forest products trade. Still, market access in regional and particularly in international markets is crucial for national economic development. In the past, boycotts of tropical timber organised by consumer groups and NGOs have impacted greatly on market access, particularly of tropical timber. However, the example of the Indonesia-UK bilateral agreement on “legal timber” imports shows that already, after the relatively short time of its existence, there is a notable shift towards less scrupulous industry conduct and an increasing sensitisation of markets on the issue of sustainable forest management.

It was stated that forest products are much more “sensitive” in international markets, particularly in Europe and North America, than regular commodities like coffee. An approach such as “Fair Trade” in organic agriculture and community-based marketing might be seen as “preferential treatment” due to international support to sustainable livelihoods and rural development. But “Fair Trade” was seen as a market-based, consumer-oriented product promotion initiative and it is not subject to the debate in trade liberalisation. It was underlined that this is different from the issue of public procurement policies which are often contentious because of possible violations of the non-discriminatory principle of the WTO rules.

The point was made that the forest industry is capacity sensitive. In the past, trade barriers have induced a large overcapacity in down-stream industry like sawmills, pulp/paper factories etc. which is of concern to those companies which are exposed to the increasingly liberalised markets. More products need to be subject to debates of import/export tariff reduction which are still rather high, particularly in tariff escalation. The major issue here is the use of various subsidies to protect domestic industries. Changing market patterns and trade flows in forest products at the international level should not be counteracted by domestic responses in terms of protectionism.

6.2 FOREST-RELATED MULTILATERAL ENVIRONMENTAL AGREEMENTS (MEAS) AND CURRENT POLICY DEBATES – BY: RUPERT SCHLEGELMILCH, EUROPEAN COMMISSION

Introduction: a sustainable globalisation

The European Union does not consider trade liberalisation as an end in itself. Rather, it is seeking rules-based market openings as access to the global market is an essential precondition for economic growth and development. A global economy needs more international rules and stronger multilateral institutions. The WTO is all about the rule of law in international trade and we have to update the rulebook to reflect the realities of the global economy. The Doha Development Agenda is essential to create the necessary balance between market access and a rules-based framework.

The bottom line is this: globalisation can be positive for all countries provided it is properly harnessed and respects all three pillars of sustainable development: economic, social and environmental. Through harnessed globalisation we can ensure that the gains from enhanced growth are spread evenly throughout global society and to ease the plight of those that have to bear the costs of sometimes painful adjustments.

This view is reflected by positions or actions taken in multilateral, bilateral fora and by the setting up of EU internal regulation.

The EU is working to promote further the contribution of trade liberalisation to sustainable development both multilaterally within the WTO, but also within the framework of fora such as the WSSD, as well as in our regional and bilateral trade relations. The promotion of sustainable forest management is an important element in this work.

The aim of this presentation is to provide a short overview of some of the activities undertaken and the challenges faced by European policy makers to reach this objective vis-à-vis trade, environment and forests.

The multilateral level: negotiations in the DDA

The EU wants the WTO to be visibly more supportive of sustainable development and sees the launch of the DDA as a key opportunity in this context.

The DDA is the best instrument to improve the participation of developing countries in the global economy and to address the impact of trade liberalisation on key non-trade objectives that our society holds dear: environmental protection, public health, consumer safety and social development. The EU attaches a lot of importance to all these issues.

On environmental protection, the DDA includes negotiations on a number of issues. Three issues in particular should be mentioned in the context of forestry; *the relationship between WTO and MEAs, MEA observership to the WTO-negotiations and environmental goods and services.*

The relationship between WTO rules and MEAs

In our view, a clarification on the relationship between WTO rules and MEAs is important as the current legal situation is creating uncertainty for trade and business and

‘chilling’ the development of environmental policy.

A clarification will make multilateralism de facto more attractive than unilateralism without changing WTO rules per se and render policy making clearer for makers of both trade policy and environmental policy alike, as well as supporting multilateral efforts to tackle international environmental problems, but opposition is widespread. A clarification would also be of particular benefit to smaller and weaker countries as they are more likely to be the objects of (and less able to resist) unilateral measures than more economically powerful entities.

MEA observer status to the WTO-negotiations

Another important issue negotiated within the DDA is the issue of MEA observer status to the WTO negotiations, as well as information exchange between MEAs and WTO of an effective and adequate international context. The expertise of UNEP and the MEAs is needed in the ongoing discussions in the WTO as these bodies are affected by the negotiations. This is an essential issue of international governance and of WTO-transparency.

The EU is therefore pushing hard for a decision already in Cancun to grant permanent observer status to MEAs and UNEP to the CTE Special Session negotiations, irrespective of the problems to solve the more difficult issue of observer status in the WTO as a whole.

Environmental goods and services

A third essential environment issue in the DDA regards enhanced market access for trade in environmental goods and services.

The EC has been strongly supporting the inclusion of negotiations on this issue as it provides scope for synergies between trade liberalisation and sustainable development. The need to promote trade in environmental goods was also emphasised in the 2002 WSSD Plan of Implementation.

The discussions on this part of the DDA mandate has so far raised a number of issues related notably to definitions of the concepts involved. There is currently no universally accepted definition of environmental goods and services and views differ between WTO-members as to what products should be considered as such. The question of whether or not to include forest products issued from sustainable forest management (SFM) in this definition has also been raised

In this context it should be noted that the discussion on the inclusion of sustainable forest products in the definition of environmental goods would be strongly facilitated if there were at our disposal internationally agreed standards for sustainable forest management which could be used as a technical reference in trade policy.

Raising trade and sustainable development issues in our bilateral and regional agreements

Bilateral relations provide a privileged frame for creating opportunities to enhance trade in forest products which are produced from sustainable forest management.

The European Commission is willing to reflect further, together with its trading partners, on how sustainable development could best be favoured using the opportunities offered through bilateral Association Agreements.

Political dialogue, cooperation and trade agreements as such can contribute to improve the contribution of new trade conditions to sustainable development.

These sustainable development related instruments are covering trade in forest products and should aim in particular at fostering trade in products specifically issued from SFM.

Bilateral relations are also a privileged place for acting against illegal logging activities with exporting countries sharing our concerns on this issue: in the framework of an action plan worked out by the European Commission (see below) we propose to set up partnerships in which enhanced technical assistance and tracking systems are implemented while a stricter control procedure makes it possible to address more effectively trade in wood products coming from illegal logging.

Using good tools:

The Generalised System of Preferences as a tool for promoting forest sustainable management

The Generalised System of Preferences (GSP) is meant to foster sustainable development by providing additional trade preferences in particular with the *special incentive for the environment*: this arrangement responds to beneficiary countries' efforts to comply with internationally agreed standards regarding sustainable forest management.

The future revision of the GSP system will certainly reinforce its role for promoting trade and sustainable development and in particular sustainable forest management.

Developing dialogue

Dialogue between trading countries is increasingly important for trade, environment and forest issues not only in multilateral fora (WWSD, UNFF) but also in bilateral relations.

This dialogue should **raise the interlocutors' awareness** of each other's concerns and contribute to a **better understanding of trade and sustainable development (SD)** issues. This kind of dialogue could contribute to building more consensual policies taking into account the concerns of each trade partner.

Recently, the EC proposed such a dialogue on trade and SD between the EU and Mercosur countries.

Dialogue proposed in multilateral fora is also important to improve our understanding of issues at stake and exchange points of view on possible actions.

Corporate Social Responsibilities (CSR) activities and public private partnerships

Complementary approaches by private and public sector have to be undertaken for enhancing the contribution of trade to sustainable development. CSR is not a substitute, but a complement to hard law. As such it must not be detrimental to public

authorities' task of establishing binding rules, at domestic and/or at international level, for the respect of certain minimum social and environmental standards.

The focus of the debate in this respect has now moved on from a simple dichotomy between voluntary and binding instruments, towards the overarching challenge of devising reporting tools and verification mechanisms to ensure proper compliance with CSR commitments

The European Commission is fully committed to promoting CSR activities in general and in particular in the forest sector: CSR is notably one of the key themes identified in the action plan proposed by the Commission to combat illegal logging.

As clearly demonstrated during the WSSD, public-private partnerships are offering opportunities which should be used for developing trade in forest products produced from sustainably managed forests.

Action plan against illegal logging:

Illegal activities in the forest sector have been emerging as a major problem in some developing or transition countries: this issue is contributing to the unsustainable use of forest resources and to forest depletion.

To combat illegal logging and the trade in illegal timber the European Commission is proposing actions around the following themes:

- Help for partner countries to build systems to verify timber has been harvested legally;
- Initiation of a voluntary licensing scheme where partner countries issue a permit attesting to the legality of timber exported to the EU.
- A public procurement policy where contracting authorities will be guided on how to deal with legality when specifying timber in procurement procedures.
- Measures to prevent investment in activities that encourage illegal logging.
- Encouragement of private sector initiatives for good practice in the forest sector, including the use of voluntary codes of conduct to source only legal timber.
- Actions to address the problems posed by the use of revenues from illegally harvested timber to fund and prolong armed conflicts.

Next steps and needs:

Need for internationally agreed standards

The non-discriminatory principle enshrined in the WTO has to be respected by any trade policy measure.

Therefore an approach favouring the use of **international agreed standard** should be preferred for promoting environmentally or SFM products.

Progress in this area is key: trade policy maker need such technical tools to base their policy decision on genuine and non controversial standards.

Better assess the impacts:

Impacts of trade opening on the forest sector and on forest management are mainly related to negotiations taking place in Non-Agricultural Market Access and Agriculture.

Assessing the global impacts of all negotiating mandates is very important in order to foresee cross-cutting effects and to be able to mitigate any negative impacts of trade policy on social development or environmental resources (in particular forests). Since 1999 the EU Commission has launched a programme of sustainability impact assessment (SIA) whose goal is to:

- Give the information to policy makers of impacts of trade negotiations on sustainable development within its three pillars (environment, social, economy)
- develop complementary tools and measures to mitigate negative impacts and enhanced positive ones.

This SIA programme and SIA methodology are work in progress. We recognise that there is room for improvement and are working to this end. The broad and open consultation process built around SIA work plays a key role for improving the whole SIA process.

An SIA on forests will be launched after the summer break. For those who are interested in participating or commenting current work, I strongly recommend to contact our external experts (IDPM Manchester <http://idpm.man.ac.uk/sia-trade/>) who will carry out this study.

We welcome any contribution or suggestions regarding our work in this field.

DISCUSSION:

Much as the FLEGT process in Asia and Africa is appreciated by a range of interest groups, it was noted that the dimension of poverty reduction has not been integral part of the initiative. While geared at compliance with national and international laws and focused on governance issues, FLEG is not intended to impose policies and pieces of legislation onto developing countries. On the contrary, participatory and partnership approaches should ensure that a broad range of constituencies and stakeholders are involved in setting positive frame conditions to increase awareness of the relevant legislation and to achieve increased transparency of operations in the forests through public debate and policy processes which are open to society.

The European Commission (EC) has always emphasised that the work on social aspects of development are crucial and will determine success or failure. Building up corporate social responsibility within the society, including the international private sector active in a given country, is amongst the most important functions of governments. However, it remains to be agreed upon within the respective national context, what the standards for compliance with the law and social responsibility for the sustainable management of forests are. Existing domestic fora such as processes of national forest programmes and other policy processes, are not yet sufficiently used for determining these standards. The discussion on standards, however, has just started and it remains to be seen where this process at the national, regional and international level will lead.

What is certain is that the next step after this determination would be the mainstreaming and application of these standards which, again, can only be achieved through informed consent within the respective society. It was noted that the issue of illegality in the use of forests and trade in forest products should also be addressed in developed or industrialised countries.

With regard to compliance with the law and good governance, it was underlined that illegality in logging and trade in forest products is relatively easy to define. However, existing national legislation might not be sufficient and policies not clear enough to effectively tackle the current problems in forest management. Ad-hoc regulations like the ban of export of logs and square logs from Indonesia to Malaysia and the corresponding directive from the Ministry of Primary Industries of Malaysia are not necessarily a solution in the long run, despite the fact that there are controversial views on their effectiveness.

It was pointed out that the Congo Basin Partnership which brings together 39 partners (governments, NGOs, the private sector) aims at bringing a solution to the improved compliance with international and national laws and better governance very close to the forests and to the management of forests. This partnership, deriving as a Type II initiative of WSSD, is an attempt to start working on the supply side of the forest products trade particularly in tropical timber rather than relying on the demand side which is active in Europe and in North America. In order to support the supply side in developing countries the question was raised whether or not the World Trade Organisation and its trade rules could possibly identify measures of a “privileged treatment” of tropical timber trade coming from legal sources and sustainable forest management. It was noted that currently the Committee for Trade and Environment (CTE) of WTO is addressing issues of market access and the role of Multilateral Environmental Agreements (MEA).

6.3 “FOREST AND FOREST PRODUCT CERTIFICATION AND ITS IMPACT ON TRADE AND TRADE POLICIES”

SUBOH MOHD YASSIN, DEPUTY SECRETARY GENERAL, MINISTRY OF PRIMARY INDUSTRIES MALAYSIA

Introduction

1. Certification has been used to indicate certain standard of achievement. It is an instrument adopted by many and applicable to our daily lives. What is important to note is that through certification the general public will be able to know that the holder of the certificate is supposed to have attained certain standards. In that regard it is a useful instrument from both the management and marketing perspective. This is also true of forest and forest products certification. As a country which is endowed with rich natural resources, the Government of Malaysia has adopted a policy of sustainable forest management. This is to ensure that the benefits which be derived from the rich natural resources can be used to meet current developmental objective but also to ensure such benefit can also be enjoyed by future generation. As a matter of fact, the first forest officer was appointed in 1901. We are happy to note that currently more than 62% of our land area is still under natural forest cover and if we include those areas under tree covers such as rubber forest and palm oil plantations, then it will become 75%. The natural resources are being harvested and process both for domestic consumption and export. In 2002 we export about RM15 billion worth of timber products. Therefore certification constitutes a very important aspect in the management of our natural resources.

Impact of Certification On Trade and Trade Policies

2. Timber certification was developed as a market-linked tool to encourage sustainable forest management (SFM) and the first certification scheme started operation in 1994. Up to May 2003, a total of 152 million hectares of forests have been certified, but this accounted for only 3.9 % of the world's total forest area of 3,869 million hectares. This figure is even lower in the case of the tropical forests, which only accounted for 6 % of the total area of certified forest. Therefore currently timber certification has still not made a significant impact in terms of the area certified.

3. Although data on the quantity of certified forest-based products being traded internationally is still quite scanty, it is likely that this quantity is currently not significant compared to the total international trade in forest-based products.

4. Nevertheless, for a country such as Malaysia, which has export-oriented forest-based industries, particularly the wood-based industries, the impact of timber certification is starting to be felt. Malaysia exports timber products to more than a hundred countries throughout the world. Among these destinations, there is increasing interest in sourcing certified timber products from the more affluent and environment-sensitive markets such as western Europe, USA and Australia.

5. In some of these markets, aggressive campaigns have been carried out by the leading environmental and social NGOs to persuade companies dealing with timber products to support certain certification scheme. As a result, many importers, retailers and do-it-yourself (DIY) companies dealing with timber products in the major developed countries have formed buyers' groups, which give preference to suppliers who are able to supply products certified under such scheme.
6. In addition to the actions taken by the buyers' groups, which comprise private sector companies, some national and sub-national governments have announced public procurement policies, which either do not accept tropical timber products or only accept them when they are certified under certain scheme.
7. When one talks of certification there are numerous certification scheme. In Europe, large areas of forests have been certified under the Pan European Forest Certification (PEFC) Scheme, which operates in most of the European countries. In addition there are NGO sponsored scheme such as the FSC; as well as, there are also national timber certification schemes operating in countries such as Canada, USA, Brazil, Chile, Indonesia and Malaysia.
8. From our perspective, we notice that all these schemes are working towards sustainable forest management. That being the case we of the view that the most logical approach would be to pave the way for closer collaboration. In this manner it will facilitate toward attaining our common objective of sustainable forest management. Such cooperation can be in the form of mutual recognition. There is tremendous scope for bringing about this kind of cooperation into reality.
9. In Malaysia, the Malaysian Timber Certification Council (MTCC) is an independent organisation established to develop and operate a voluntary national timber certification scheme.
10. The MTCC timber certification scheme began operation in October 2001 using a phased approach. As a matter of fact the ITTO at its recent council meeting recognized this approach. The standard currently used for assessing Forest Management Units (FMUs) for the purpose of certification is the *Malaysian Criteria, Indicators, Activities and Standards of Performance for Forest Management Certification (MC&I)* which is based on the 1998 ITTO *Criteria and Indicators for Sustainable Management of Natural Tropical Forests*.
11. In response to the market requirements, for the next phase of its certification scheme, MTCC will use a new standard that has been developed through multi-stakeholder consultations, using the Principles and Criteria of the FSC (a well known NGO sponsored scheme) as the template.
12. In view of the existence of numerous international certification schemes such as the PEFC, FSC and various national schemes, it is felt vital to work toward mutual recognition. As had been indicated earlier what is important is that all the scheme are working towards achieving sustainable forest management and therefore the need for promoting collaboration, cooperation, rather than competition.

Issues of Forest and Forest Products Certification

13. In discussing forest and forest products certification, there is a need to distinguish between two different objectives for interested parties to advance the issue of product certification. On the one hand, it is legitimate for certification to satisfy the consumer's demand for more information on the product in order to help him in making the decision whether or not to purchase a particular product. On the other hand, those with interest in promoting the usage of certification to advance the policy agenda towards greater protectionism for the trade agenda is a different matter altogether. Therefore the challenge for policy-making and trade policy is to ensure that certification serves the legitimate objective of informing the consumer and not allowing the usage of certification as a front for unjustifiable protectionism purposes or for unreasonable agenda.

14. Discussions at this roundtable could address some of these questions and issues i.e. how do we negate the likely resort to this instrument for protectionist purposes? How do we avoid the creation of a monopolistic situation and its attendant negative implications on trade in forest and forest products? And how do we prevent abuses of the use of this instrument for the promotion of certain policy agenda?

15. In pursuing the legitimate objective of consumer information, Malaysia does not want this objective to be abused under the guise of protectionism. Although, certification is still voluntary at this stage, nevertheless it poses concerns especially from developing countries.

16. Additionally, certification has other trade implication, as it would be burdensome and costly especially for developing countries to meet additional requirements. Based on Malaysia's experience, in drawing up the criteria and indicators for certification, it is not only burdensome but involves additional expertise in terms of new technology, manpower, time and cost. Some of these criteria are very subjective, leaving room for different interpretations. These obligations would introduce arbitrary and unjustifiable trade measures more restrictive than necessary. Hence, these would inevitably constitute and create unnecessary barriers to trade. The cost of compliance for exporters creates a barrier to trade. Therefore Malaysia, and I am sure that many developing countries in a similar situation as well, would have serious concerns about the potential adverse impact of certification on exporters and trade in general.

17. Furthermore, through timber certification, it is envisaged that consumers would be able to discriminate between timbers emanating from sustainably managed sources and those derived from destructive or 'unsustainable' sources. In theory, at the very least, it would have the advantage that it would provide timber producers with an incentive to improve forest management practices, comply with agreed standards, gain certification, and sell products at a premium price, assuming consumers would be prepared to pay a higher price for a 'green' product.

18. In this context, studies conducted in Europe on willingness to pay a 'green' premium for forest products emanating from certified forests indicate that consumers are not very willing to pay.

This is also true for the United States where 81 and 70 percent of the companies that own and manage forest lands and companies that manufacture and sell certified products but play no role in the management of forest lands, respectively, are sceptical that any premium will emerge. This is not surprising as it is well-known phenomenon in marketing that any 'new products' coming into the market would generally command a higher price and once supply moves towards meeting demand, the prices will drop rather quickly and be stabilized.

19. We are also of the view that by providing better market access for such products would contribute toward avoiding over-exploitation of these natural resources. Though certification is supposed to be voluntary, market demands by certain developed countries have made it a requirement for market access. Indeed certification is now used as a non-tariff barrier by not only local authorities but even by national governments. Public procurement policies have been promulgated to restrict the use of tropical timber, which do not come from sustainably managed sources. This certainly goes against the very agreement that many Governments have made that timber certification is voluntary and that tariff and non-tariff barriers to timber trade should be reduced or removed.

20. In discussing the impact of certification on trade, it must also not be forgotten that for many developing countries, the achievement of SFM, which is the prerequisite for a certification scheme, is itself a huge challenge.

21. In the developing tropical producer countries, resources are limited and SFM is not given such a high priority in the national agenda due to other competing and more pressing social and economic needs. Consequently the financial and human resources needed to achieve SFM are not readily available in these countries. Under such circumstances, there is great difficulty in achieving SFM, and consequently timber certification cannot be implemented.

22. It could also be argued that for many developing countries, meeting the basic needs of development in order to address poverty and the problem of food security is a national priority. The Convention on Biological Diversity in its preamble recognizes that States have sovereign rights over their own biological resources and this was reaffirmed in the World Summit on Sustainable Development in Johannesburg. This would include the rights on how to develop them in a responsible and sustainable manner. In many cases, through the development of the natural resources is the only means and comparative advantage developing countries have in securing necessary foreign exchange to satisfy this basic need. Imposing higher environmental standards through certification requirements or other conditionalities would be chaining these countries to the shackles of poverty forever. Countries need to determine their priorities in the context of their national objectives, circumstances, legislations and needs.

23. Instead of imposing further obligations on developing countries, to encourage industrial development and further downstream activity of these natural resources, market access improvements through tariff reductions and elimination of tariff escalation on processed products in the forestry sector should be undertaken as a matter of priority in the context of the World Trade Organization (WTO) negotiations.

It is recognized that economic development goes in tandem with higher levels of achievement in environmental protection.

24. In addition, the management of tropical forests is much more complex compared to the temperate and boreal forests. Considerable resources are needed especially by the developing tropical timber producer countries to improve forest management practices to the level required for forest management certification, where the economic, environmental and social aspects of forest management must be taken into consideration in a balanced manner.

25. These difficulties are further compounded by unrealistic demands from certain quarters, both within and outside the countries concerned, when the standards for forest management certification are being developed. There seems to be a tendency to expect all the problems related to forest management will be solved through timber certification, when it is clear to us that some of these problems are cross sectoral in nature.

26. The difficulties faced by developing countries in implementing timber certification or in getting their certification schemes recognized by the international market are therefore of great concern and must be taken into account when discussing the impact of certification on trade.

27. Furthermore, no green premium is paid by the market for certification and Third World countries have to bear the additional costs. Indeed, with few developed countries delivering their commitments on new and additional financial resources to assist developing countries to implement SFM, it is tantamount to poor countries having to bear the burden of implementing SFM, the benefits of which are global in nature and accrue to the rich as well.

28. Further we are also of the view that if our partners in the developed countries are sincere in wanting to assist Third World countries to achieve sustainable forest management then they should not be loading additional conditionalities for Third World forest products to comply with, as it will only make it unsustainable for developing countries to even implement the basic elements of SFM. Indeed in handling such issues, dangling the carrot would be the better approach than wielding the stick.

29. Malaysia would also like to support full cost internalization of forest management. The non-monetary and non-marketable outputs and benefits of the forests should be valued and compensated for by consumers. Presently the market pays only relatively low prices for forest products without any compensation for non-timber functions that forests provide to the world in terms of its biodiversity, carbon sequestration and clean air. Nor does the market place pay for the cost of sustainable forest management. Full cost internalization will reflect the true value of forests and its multiple functions and contribution to mankind. It is therefore justified that the global community, particularly the rich developed but forest-poor countries should compensate forest-rich countries in the developing world for providing those functions.

Conclusion

30. Hence the issue of certification requirement should be tackled together, as part of a whole package, and not in isolation but linked with adequate compensation for non-timber functions as well as other issues of market access, mutual recognition of certification bodies, capacity-building and technology transfer. By adopting an integrated approach in a holistic manner, only then can we hope to minimize the negative impact of forest and forest product certification on international trade. Thus the challenge lies for policy makers to balance the need to satisfy consumer information and how to prevent abuses through the usage of certification to promote the advancement of certain policy agenda of interested groups.

Discussion:

It was noted that forest products certification does not pay! Niche markets for specific products are available to a much lesser extent than anticipated. However, forest products certification has a long standing history in standard setting for sustainable forest management and can be looked at as an effective instrument to support C&I processes and governmental policy making in involving a broader set of stakeholders in the debate. However, with regard to market access, particularly for tropical timber and plantation wood, domestic public policies and institution building are geared at emerging national certification schemes.

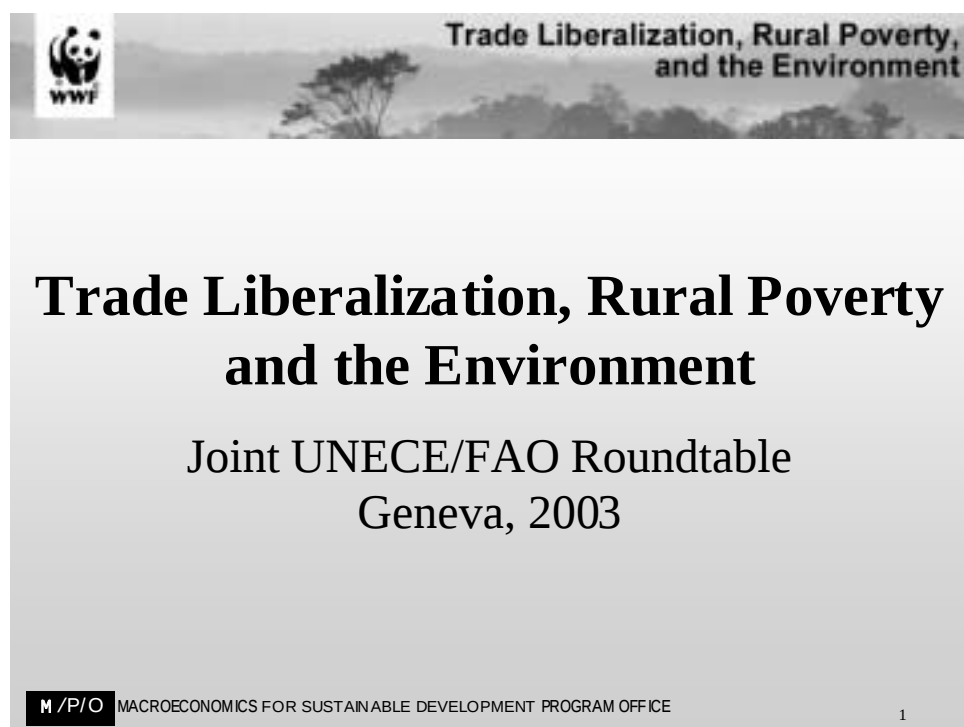
To date, forest products certification has in effect not greatly influenced markets for forest products and trade dynamics, even though campaigns have been sensitising consumers. Surveys show, however, that consumers are still not in a position to distinguish between the various certification schemes and their labels, even though the overall objective of all schemes, namely SFM, is supported by most.

Environmental NGOs greatly appreciate forest certification as a tool to introduce ecological and social standards in forest management approaches and forest industries conduct and practices; however, proliferation of certification schemes and their labels is not the major problem today, but the competition between the different schemes in the market place for forest products. Since forest certification and chain-of-custody verification is supposed to be a market-based instrument, it appears as if this approach is not subject to WTO negotiations given the fact that forest certification is voluntary and labels should not be government induced or based on any domestic legal provision. On the other hand, the currently discussed “legality certificate” for forest products which is meant to be issued by governmental authorities is of increasing concern to producer countries, particularly in the tropics. It is seen by some governments as part of the future approach to forest certification and chain-of-custody verification possibly constituting an important non-tariff barrier which decreases market access and decreases the opportunities to achieve sustainable forest management.

With reference to the CTE Report to WTO Ministerial Conference in Cancun, it was outlined that despite the fact that forest certification is designed as a market-based instrument, many governments regard the approach as a non-tariff barrier in forest products trade aiming at international standards rather than a loose set of recommendations for SFM. However, voluntary certification in forestry is per se not an issue of concern to WTO. Public procurement policies, technical barriers to trade (TBT) etc. should be clearly distinguished from current forest certification.

7. Session II – Impacts of Trade in Forest Products and Services

7.1 TRADE, RURAL POVERTY AND THE ENVIRONMENT – BY: OWEN CYLKE, WWF US





Trade Liberalization, Rural Poverty,
and the Environment

Rural Poverty and Forests

Conceptual Rationale

Cause of the problem:
“downward spiral”

Solution to the problem:
“synergy” between economic development,
poverty reduction and forest conditions

M/P/O MACROECONOMICS FOR SUSTAINABLE DEVELOPMENT PROGRAM OFFICE 3



Trade Liberalization, Rural Poverty,
and the Environment

Rural Poverty and Forests

Pragmatic Rationale

- without the connection to rural peoples, poverty reduction becomes rationale for deforestation
- without the connection to rural peoples, protection of forests probably not sustainable
- without the connection to rural peoples, unlikely buy-in from the South

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Trade Liberalization, Rural Poverty,
and the Environment

Rural Poverty and Forests

Ghost Trade

- on-farm and local benefits
- regional and national benefits
- global benefits
- “ghost trade”
- legitimizing the trade in forest services

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Trade Liberalization, Rural Poverty, and the Environment

Trade Liberalization

Conventional Wisdom <i>North</i>	The Record <i>South</i>
• economic benefits • development benefits	• income distribution and equity • investment • trade specialization

M/P/O MACROECONOMICS FOR SUSTAINABLE DEVELOPMENT PROGRAM OFFICE 6

Trade Liberalization, Rural Poverty, and the Environment

Divergent paths of developing countries in the 1990s
(GDP per capita growth rates)

Category	Growth Rate (%)
Marginalized countries	-0.5
Rich countries	1.5
Globalizing developing countries	4.5

Foreign Direct Investment

Category	FDI (Millions of USD)
Marginalized	5,000
Globalizers	15,000
OECD	45,000

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Trade Liberalization, Rural Poverty, and the Environment

Why then the emphasis on trade?

- Havana Charter
- Monterey and Johannesburg
- Washington Consensus
- WTO - Beyond Borders

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The Real Trade Agenda

- development and sustainability objectives (national)
- political economy (national)
- trade policy (national)
- trade rules (international)
- new trade agenda
(competitiveness, investment, technology)



Problems with the WTO Agenda

- the process - backwards (rules, policy, objectives)
- a mercantilist culture (finance over economics and ecology)
- absence of safety nets (Washington Consensus)
- “spaces for development policy” (ICTSD)
- governance (“by invitation only”)



What Room for the Market?

- ecology and economics (different worlds)
- certification - water pricing
(promising synergy)
- governance
(making trade-offs explicit)

DISCUSSION:

In the brief discussion, it was outlined that the debate around trade liberalisation does not leave enough room for development policy making. Liberalised trade and economic growth dominate the international agenda and development under certain circumstances, particularly in the developing world becomes environmentally destructive. Trade liberalisation is neither the answer to development problems nor is it to be seen as a “stand-alone” policy issue while environmental concerns are addressed under a different set of policies and other legislative provisions. The interactions and impact between trade (liberalisation) and sustainable development, notably sustainable forest management, should be further analysed.

Even though foreign direct investment (FDI) has been rising in certain parts of the developing world, trade liberalisation is not likely to happen in those countries without the support of overseas development assistance (ODA). It was reiterated that WTO never had a development agenda, but member states agreed that liberalised trade would be generally supportive of development issues. Trade rules are therefore not made for the protection or sustainable use of the environment and natural resources.

It was stressed, however, that WTO negotiations have come to a point where the distinction between the current developments in liberalised trade and approaches to address environmental concerns, including the sustainable use of natural resources can no longer be upheld. The current discussion in the Committee on Trade and Environment (CTE) of WTO on the issue of influence of multilateral environmental agreements (without containing obvious “special trade obligations” (STO) like CITES) shows quite clearly that there is a growing awareness in the international community of environmental and social concerns beyond the issue of non-tariff barriers which could be erected based on issues unsolved in sustainable development which is meant to be economically viable, but also environmentally sound and socially appropriate.

**7.2 MARKETS FOR FOREST ENVIRONMENTAL SERVICES –
BY: MARKKU SIMULA, INDUFOR FINLAND**





Main Environmental Services of Forests

- **Services**
 - biodiversity
 - carbon sequestration
 - watershed protection
 - forest landscape beauty
- ⇒ **Major opportunities to promote sustainable development through trade**
- ⇒ **Implications need to be clarified and stakeholder concerns addressed**

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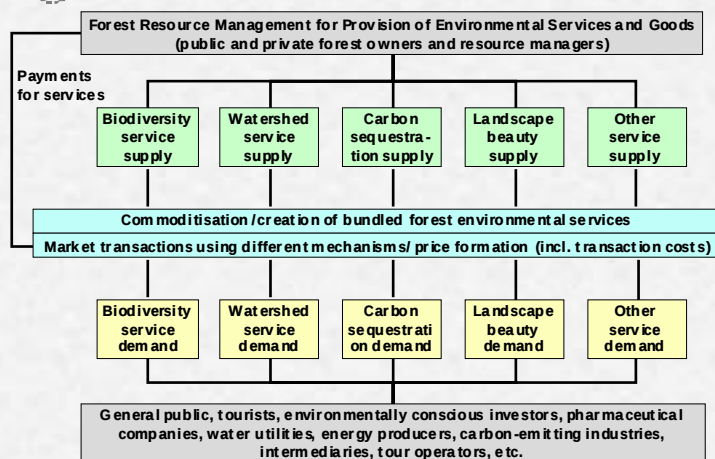
Linkages With Trade Negotiations

- **definition of environmental services**
- **implications for sustainability**
- **potential conflict between CDM and WTO**
- **subsidy issue**

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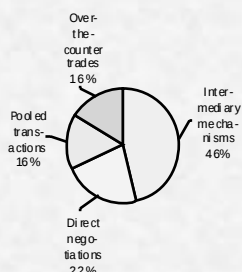
Market Framework



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Market Mechanisms for Trading Environmental Services of Forests



Other mechanisms:

- investment funds
- venture capital
- intra-corporation trading
- joint ventures
- clearinghouse transactions
- auctions
- retail trade
- commodity exchange
- etc.

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Market Creation Factors

- demand and supply potential
- value and significance of the service
- geographic location of the market
- commoditisation potential
- easiness of defining and enforcing property rights
- degree of excludability and rivalry of the service provided
- transaction costs
- scientific uncertainty and verification possibilities
- risks

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Carbon Sink Projects in 2003

Region	Project type			Total
	Afforestation and reforestation	Combined	Forest protection, conservation and management	
	1000 ha			
Latin America	180.6	590.4	3 407.9	4 179.0
Africa	43.4	..	476.0	519.4
Oceania	166.5	..	..	166.58
Europe	39.3	24.1	63.5	63.5
Asia	2.4	14.0	2.0	18.4
North America	5.7	0.5	..	6.2
International	..	..	..	..
Total	488.0	629.0	3 949.4	4 952.9
% of projects	41.3	17.4	41.3	100.0
Projects	45	19	45	109
% of total area	8.8	12.7	79.7	100.0

⁽¹⁾ The figures are based on data provided by projects and may not always be accurate. For some projects no area data was available.

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Biodiversity

- no statistics on the existing volume and value of the markets for forest biodiversity services
- proliferation of market-based schemes suggest markets have grown rapidly
- powerful demand drivers (increasing public awareness, economic growth, increasing scarcity of biodiversity, limited resources of governments, and increasing private investment)
- supply drivers (innovative mechanisms for commoditising biodiversity and development of new payment mechanisms that reduce transaction costs)
- supply outstrips the willingness to pay for conservation and competition in supply dampens payments for conservation

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Water

- upstream action generates downstream benefits that the beneficiaries pay for
- existing markets are modest and local
- payment schemes are confined within national boundaries
- market development is subject to many uncertainties
- demand drivers (failure of regulatory measures and continued degradation of watersheds)
- main demand constraint is lack of scientific evidence on the contribution of forests to watershed services
- the world's watersheds cover large areas but only a fraction could become part of service arrangements

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Landscape Beauty

- markets are linked with amenity values and development of tourism and recreation
- value of broader landscapes for local people and tourism has been recognised
- nature-based tourism will provide increased financing to protected area management, but government will remain the main source
- market for landscape beauty is large and expanding
- problem lies less in market creation than in ensuring that protected areas are able to capture a fair share of the benefits

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Verification of Environmental Services

- **markets will require verification of environmental services to achieve credibility**
- **third-party certification would garner public confidence and credibility**
- **payments for services call for transparency and accountability**
- **verification /certification would add to the transaction costs**
- **certification of bundled services (joint production of different environmental services) could reduce transaction cost as linking service verification with SRM certification**

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Impacts of Trade and Sustainable Forest Management

- **markets for forest environmental services are nascent**
- **carbon offsets from forests have the largest potential to become a globally traded environmental service**
- **incremental impacts of other environmental service markets on wood supply and prices, and thus on international trade flows, are likely to be insignificant**
- **government interventions are needed through an appropriate balance between regeneration and market forces**
- **benefits should flow to producers of services**

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Policy Issues

- **definition of forest environmental services under the WTO agreements**
- **payments for trade or subsidies**
- **national trade policy and market development to promote environmental services**
- **trade in forest products and environmental services**
- **promotion of SFM through sustainable development**
- **mitigation of the sovereign risk**
- **clarification of environmental services in international trade statistics**
- **measures to support capacity building of developing countries**

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FAO Round Table
Trade, Environment and Forests Working Together for Sustainable Development
Geneva, Switzerland, 9 July 2003

**MARKETS FOR ENVIRONMENTAL SERVICES -
IMPACTS ON TRADE IN FOREST PRODUCTS AND
POTENTIALS FOR SUSTAINABLE FOREST MANAGEMENT**

Markku Simula
Indufor Oy

INTRODUCTION

Sustainability of forest management involves additional costs to duly address the related environmental and social impacts but conventional markets for timber and non-timber forest products have been resistant to pay for such costs. As forests provide a full range of environmental services considerable expectations have emerged that these services could make sustainable forest management (SFM) financially viable.

Markets do not exist for these services as they have been public goods with significant elements of non-rivalry and non-excludability. Environmental services have been considered externalities which are not duly taken into account in resource allocation. Such market failures have resulted in under-production of watershed and biodiversity services or carbon sequestration. Trade – if markets can be developed for environmental services – could address these problems while more revenue would flow to landowners and communities in rural areas contributing to poverty reduction.

Liberalisation of trade in environmental goods and services can be seen as an opportunity to promote sustainable development. On the other hand, the implications of the trade have to be clarified and legitimate stakeholder concerns have to be addressed before this becomes a reality.

What are forest-based environmental services

In addition to a broad range of various goods, forests provide many ecosystem services which are categorised as environmental services. They can be related to regeneration of natural resources, stabilisation processes and life-fulfilling functions. From the trade's point of view we can break down these services into four main types:

- biodiversity
- carbon sequestration
- watershed protection
- forest landscape beauty

Linkages with trade negotiations

The WTO agreements, including GATT and GATS, do not define “environmental goods” and the definition of “environmental services” is limited to end-of-pipe activities, not explicitly covering sustainable management of natural resources. The coverage of trade negotiations remains uncertain in this respect. Definitions will have implications for the competitive advantage of environmental goods and services, national sovereignty in regulating environmental service and good delivery (sustainable development), and the nature and level of service provision (e.g., marketing of shade-grown coffee or eco-labelled forest products). Definitions may also influence the competitiveness of individual countries in the production of wood and non-wood products.

The end-use approach, using OECD definitions, includes sustainable forestry, ecotourism and potable water as separate service categories. A broader approach to include goods made in an environmentally sound manner has been advocated by some parties. Countries and stakeholders have differing views on how environmental goods and services should be defined in the WTO context.

Carbon, biodiversity and water services of forests may be significantly affected by the Doha Round. As regards carbon, the main issue is the potential conflict between the still-evolving rules for CDM-based emission trade under the Kyoto Protocol and the WTO, particularly GATS. How this potential conflict is addressed could have major implications for how CDM projects are implemented. The potential impacts of including the protection of biodiversity and landscape as environmental services in the WTO definitions are not yet adequately known and stakeholders have different views on them. In the area of water, the key issue has been opening service delivery to international competition. Defining water resource as an environmental service would broaden the view making watershed management an environmental service subject to GATS regulations.

Many definitional proposals are vague and do not allow a ready assessment of their relevance for markets for forest-based environmental services and sustainable forest management. Most of the debate has focussed on services associated with successful delivery of environmental goods, e.g., design, consultancy or research services to support investments in environmentally friendly technology. A broader interpretation of environmental services would open scope for other concerns and further studies would be needed to properly understand the potential implications of various options of defining and classifying environmental goods and services related to natural resource management.

Finally, there is the issue of whether payments for environmental services made by the public sector should be considered subsidies.

Potential for International Trade and Market Development in Forest-based Environmental Services

MARKET MECHANISMS

Markets are bringing together a buyer and seller so that they can trade commodities, be they services or goods. Direct transactions are obviously quite different from other market-based mechanisms such as taxation or subsidy schemes. The basic requirements for environmental services markets to develop are that demand either exists

or can be created, a price or value can be established for a forest ecosystem service, and that suppliers (landowners, resource managers, etc.) are able to produce and sell this service to buyers. In addition, a link between buyer and seller is required to allow exchange of information and drawing on various sources of funding. Markets can be defined at local, regional or international level which has implications for how market failures can be rectified. Environmental services can be traded individually or as a bundled commodity. A whole range of mechanisms exists for market-based transactions but it is obvious that markets are not the sole solution for sustainable delivery of forest environmental services.

A large number of different market-based mechanisms or have been promoted for trading environmental services of forests. They reflect differences in the nature of environmental services or goods and the level of market sophistication.

According to the recent study by IIED, various intermediary mechanisms through NGOs, trust funds, etc. are dominating (35% of all the cases reviewed), followed by direct negotiations between seller and buyer (17%), pooled transactions (12%) and over-the counter trades (12%). Other options include investment fund/venture capital, joint ventures, clearing house transactions, auctions, commodity exchange etc. As a whole, market mechanisms for forest environmental services are not yet well-developed. Governments, NGOs and various funds, such as GEF, are still playing a central role in intermediary and direct negotiation-based transactions, and spontaneous (free) market formation is less common.

Various mechanisms rely on different degrees of private sector involvement. In the one end of the market continuum, there are *private deals*, which require only a limited amount of public sector involvement. In the other end, public, *non-market transfer payments* for environmental services are applied. In between, one can find formal *public-private sector arrangements* or open private trading based on government-organised markets driven by market regulations (e.g. setting of caps).

MARKET CREATION

The potential of various environmental services for market development varies considerably, because some services lend themselves better for trade, whereas in some cases supply can be best ensured through instruments such as taxation and government regulation. Many factors influence market creation for environmental services such as (i) demand and supply potential, (ii) value and significance of the service, (iii) geographic location of the market, (iv) commoditisation potential, (v) easiness of defining and enforcing a property right, (vi) degree of excludability and rivalry of the service provided, (vii) transaction costs, (viii) scientific uncertainty and verification possibilities, and (ix) risks. The length of the list and the nature of the themes suggest that market creation for environmental services is a complex process.

CARBON

Under the UNFCCC and the Kyoto Protocol, a considerable effort has been made to define provisions for carbon sequestration in national GHG accounting. However, the rules under the CDM are still to be agreed upon. Trade development in the forest based carbon services has therefore suffered from significant uncertainties and remained

limited. Nevertheless, there are about 110 projects covering a total of about 5 million hectares of which most are related forest conservation, which is not an eligible activity during the first commitment period. Another observation to be made is that 85% of the area covered by carbon sequestration projects is found in Latin America. The situation is expected to change and carbon sequestration will probably be the most significant forest-based environmental service in terms of international trade. New projects would be focussed on the two eligible activities, i.e. afforestation and reforestation.

So called LULUCF (land use, land use change and forestry) activities, properly planned and under right conditions, can both store atmospheric carbon and provide other environmental benefits, such as biodiversity conservation and watershed protection. Carbon market could thus indirectly contribute to the promotion of SFM, based on multiple forest services. However, under the current rules, the Kyoto Protocol “misses” an opportunity to contribute substantially to the protection of biodiversity and watershed values associated with natural forests in the developing countries, because they are excluded from an international carbon sequestration market. At the same time, an opportunity to provide financial incentives for adopting SFM practises to provide multiple environmental services is not fully utilised.

BIODIVERSITY

There are no quantitative statistics on the existing volume and value of the markets for forest biodiversity services and only some indications of the importance of specific markets can be provided. The proliferation of market-based schemes and data on increased private sector financing for delivery of biodiversity services suggest that these markets have grown very rapidly recently and that this trend is likely to continue. There are powerful demand drivers in play that support this conclusion:

- increasing public awareness about the importance of biodiversity will enhance people's willingness to pay for conservation,
- economic growth and increasing income levels (mainly in developed countries) contributing to the willingness to pay for biodiversity services,
- increasing scarcity of biodiversity due to deforestation and forest degradation
- limited resources of governments address biodiversity problems,
- increasing private sector investment into biodiversity for a variety of reasons.

The main supply drivers are innovative efforts aimed at commoditising biodiversity and development of new payment mechanisms that reduce transaction costs. As a whole, the supply of conservation opportunities still far outstrips the willingness to pay for conservation. High levels of competition in supply, i.e. between projects available for funding, and relatively low competition in demand, tend to push the payments for conservation low, barely above the opportunity cost of land. This suggests that more emphasis must be paid to measures that strengthen the demand-side to enhance competition and willingness to pay for biodiversity.

WATER

Watershed services are one of the first forest environmental services that were seen to have potential for market-based transactions. The basic notion, where upstream

action generates benefits downstream, and the beneficiaries pay for the service, is easy to understand and can be readily accepted. The existing markets for watershed services are, however, modest and local, often involving watersheds that supply nearby urban or rural settlements. Typically, payment schemes are confined within national boundaries.

The future development of markets for forest-based watershed services is subject to many uncertainties. Currently, the main drivers behind demand are the failure of regulatory measures to accomplish adequate protection of watersheds, and continued degradation of watersheds, which is increasing their scarcity. It is therefore likely that the market expansion will continue.

A number of factors are constraining demand, in particular lack of scientific evidence on the contribution of forests to watershed services. While the perception that forests have a number of positive impacts on watershed protection is widespread, there is limited scientific evidence to support it.

While the total area of the world's watersheds is large, only a fraction of them could become part of environmental service arrangements. If the current projections of increased scarcity materialise, watershed services will gain substantially in value and give a boost to the development of market-based watershed mechanisms.

LANDSCAPE BEAUTY

Markets for landscape beauty have existed for a long time, and they are intimately linked with amenity values and development of tourism and recreation. In the past the focus was on landscape objects but more recently, the value of broader landscapes for local people and tourism has been recognised, and these values are being brought under protection. There is clearly an increasing demand in some of the wealthier countries.

The overall growth of nature-based tourism will provide increased financing to protected area management, but the present trends suggest that government budgets will remain the main source of revenue, at least in the short and medium term. However, the market for landscape beauty is large and expanding. Given the rapid growth of nature-based tourism, the problem lies less in market creation than in ensuring that protection or conservation areas are able to capture a fair share of the benefits associated with this development.

The supply of landscape beauty through subsidy systems similar to those applied in Europe is subject to controversy and may be restricted in the future. This issue has been raised in the current round of WTO negotiations and some members have challenged them suggesting that such payments are an indirect subsidy to agriculture.

VERIFICATION OF ENVIRONMENTAL SERVICES

The expansion of markets for other environmental services will require verification to achieve adequate credibility of the service delivery. Independent third-party certification would help land managers garnering public confidence and credibility, and also payments for services call for transparency and accountability. Private investors or other beneficiaries will want to know that they get what they pay for. On the other hand, verification/certification would add to the transaction costs, and consequently reduce the market opportunities.

Certification of environmental services would make sense, especially when bundled services are provided, i.e. in the case of joint production of different environmental services from forests. This would reduce transaction costs and, at the same time, facilitate marketing of multiple services. Linking verification of environmental services with SFM certification is another option to reduce transaction costs.

Impacts of Environmental Services on Forest Products Trade and Sustainable Forest Management.

Markets for forest environmental services are still relatively nascent so the level of impacts on forest products trade (e.g. plantations for carbon sequestration) will be a factor affecting whether any of these markets take off on a large scale.

Carbon offsets from forests have the best potential to become a globally traded environmental service. With regard to impacts on trade in forest products, reforestation and afforestation projects will expand the timber supply, mainly in tropical countries, and to a lesser extent, the energy cost effect will influence the location of processing industries. Use of bio energy promoted by the provisions of the UNFCCC and the Kyoto Protocol will increase wood demand for this purpose giving a boost to efficient use of forest harvest and processing residues.

The incremental impacts of other environmental service markets (biodiversity, landscape beauty, and watershed management) on wood supply and prices, and thus on international trade flows, are likely to be insignificant. However, local impacts can be important, including closing of production facilities because of reduced wood supply. The emerging markets for forest environmental services will offer an opportunity for low-income forest owners and managers to benefit economically from good husbandry or stewardship of their forest resources.

Markets cannot develop and operate without government interventions. In fact, international environmental agreements/regulations have a strong potential to increase demand for services generated by sustainable forest management. Markets and state regulation are both needed; the question is about the balance between the two, and about the strengths and weaknesses of the market mechanism. Unless market creation for forest environmental services succeeds in generating more revenue than the total market costs, and this “profit” is channelled equitably to the land stewards, the incentives for SFM will not be created.

Policy Issues

The following key issues should be addressed to make MES work effectively towards sustainable development in rural areas.

- (i) How should forest environmental services be defined under the WTO agreements as this will have impacts on demand for services and thereby for their property and use rights. The key issue is the potential conflict between the interests of local stakeholders and those of external investors and beneficiaries.
- (ii) Are payments made by the public sector for environmental services (e.g. for biodiversity or landscape) considered subsidies (falling under the WTO Subsidies Agreement), or remuneration for verifiable services produced by landowners.
- (iii) What kind of national trade policy and market development could promote environmental services, either as individual commodities or through a bundled concept.
- (iv) How could trade in forest products and environmental services promote SFM (e.g. through certification and labelling).
- (v) Should the provision of forest environmental services be subjected to sustainable development, and if so, how this could be operationalised.
- (vi) How could the sovereign risk in markets for forest environmental services be reduced e.g. by clarifying and agreeing on the basic rules for trade, including the measurement and verification methods and treatment of additionalities and baselines, leakage and permanence.
- (vii) How should environmental services, especially different types of carbon offset credits, be classified in international trade statistics.
- (viii) What measures should be taken to support the capacity of developing countries to promote forest-based environmental services.

Discussion:

It was noted that the modalities for carbon sequestration as an environmental service of forests still needs final regulation under the FCCC and it remains to be seen what the agreement of the CoP in November 2003 will be. While other environmental services like water and biodiversity are clearly defined as objectives and a contribution to sustainable forest management, the “landscape beauty” was clarified as a service aiming at recreation or eco-tourism and landscape rehabilitation. Reference was made to the financing system of Costa Rica, where landscape beauty also features as the conservation of the national heritage of natural resources.

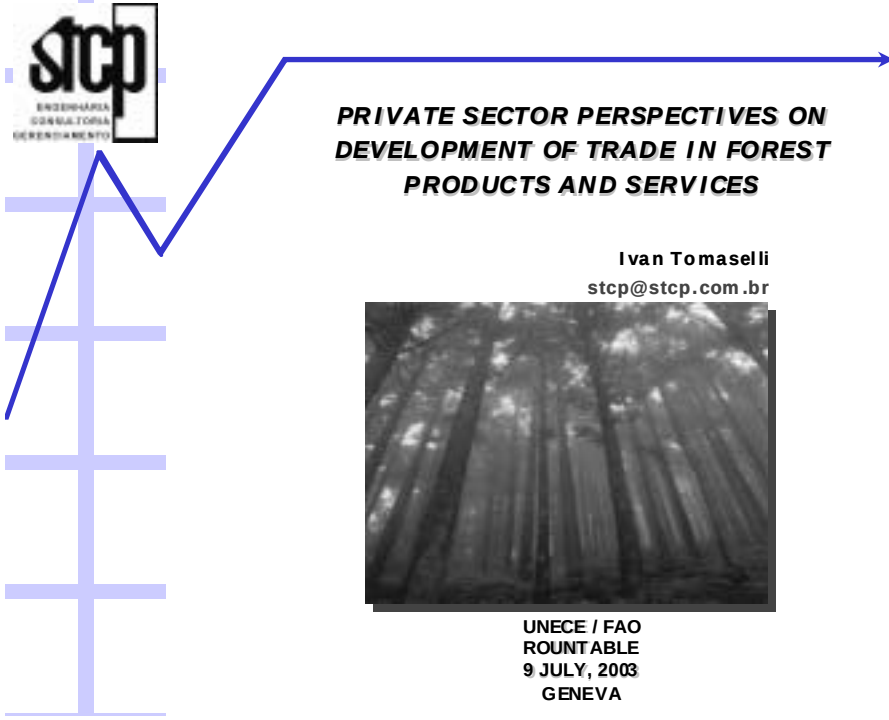
Discussions circled around the development of markets. While the presentation had focused primarily on international market development, it was underlined that national and sub-national markets play the most prominent role for example for water. Watershed management has been high on the agenda of the forestry sector since the beginning of regulated forest management and policies in this regard have been developed in almost all countries. Carbon sequestration, however, will be subject to international market development.

With regard to the creation of markets, for example for biodiversity conservation, the situation is quite complicated. The service of biodiversity conservation in protected areas and also in production forests does not suffer from plentiful supply, but is limited internationally and nationally by the demand. Therefore, market creation for biodiversity services is difficult to predict. This service is regarded as a public good for which market forces and price development are presently not applying given the fact that there is no balance of supply and demand. However, major investments by governments and NGOs into this service show different types of mechanisms and dynamics. Consequently, the definition of a “market for biodiversity conservation” and its development should be seen in the light of the overall “development market place”.

The presentation clearly showed that the internalisation of so-called externalities like environmental services, their supply and demand as well as the development of markets and prices still need a lot of development until environmental services become tradable commodities. It remains to be seen whether or not individual environmental services will find markets or whether or not so-called bundled services can be offered in order to increase the benefits of forest production beyond timber and non-wood forest products.

7.2 PRIVATE SECTOR PERSPECTIVES ON DEVELOPMENTS OF TRADE IN FOREST PRODUCTS AND SERVICES

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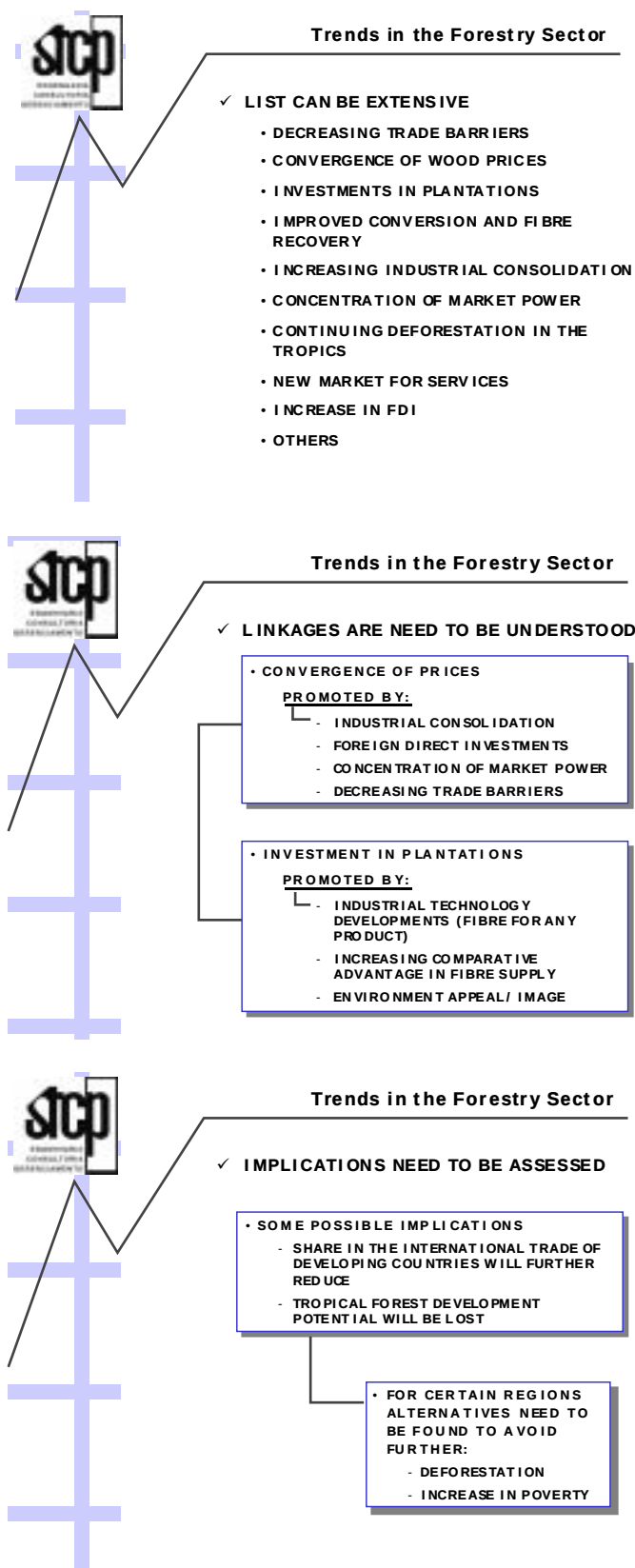


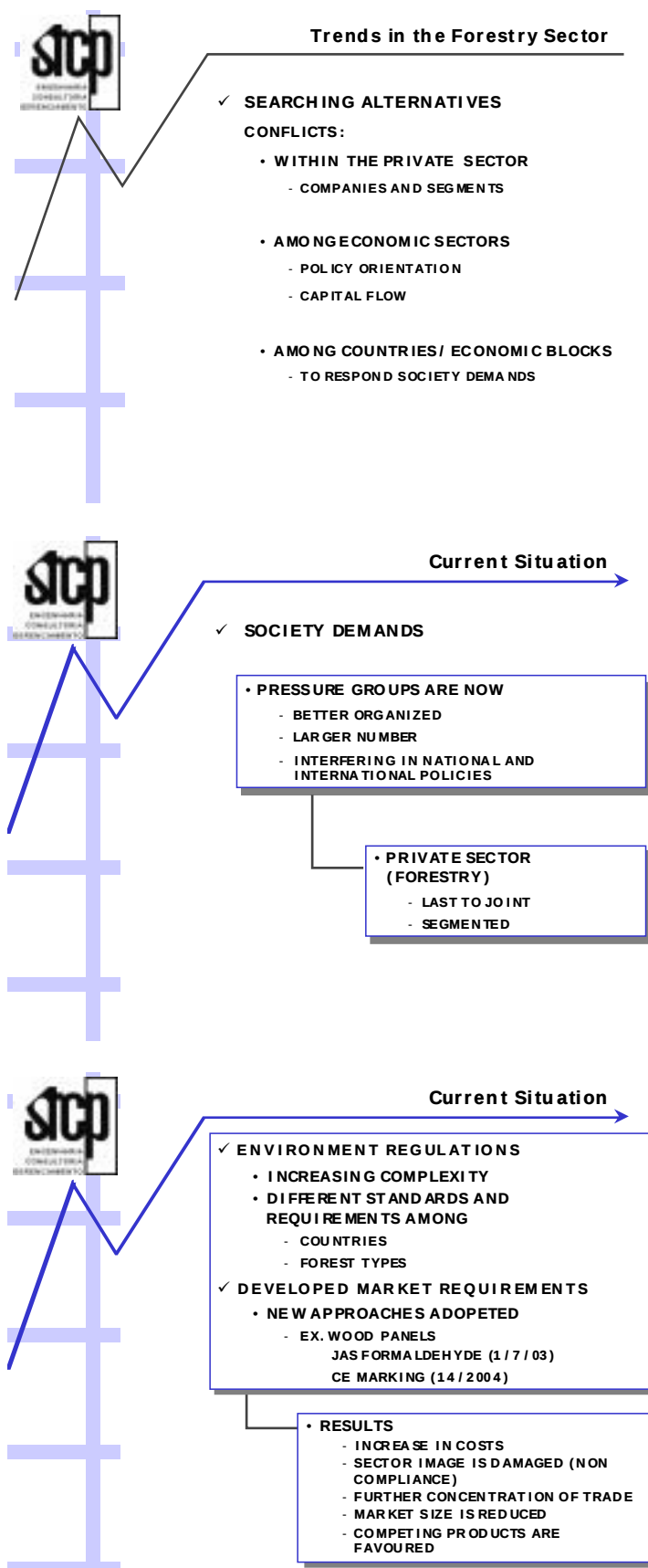
***PRIVATE SECTOR PERSPECTIVES ON
DEVELOPMENT OF TRADE IN FOREST
PRODUCTS AND SERVICES***

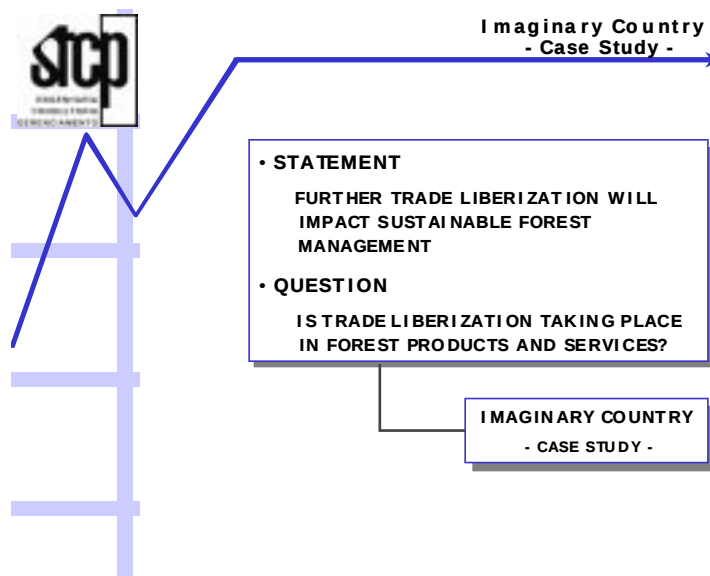
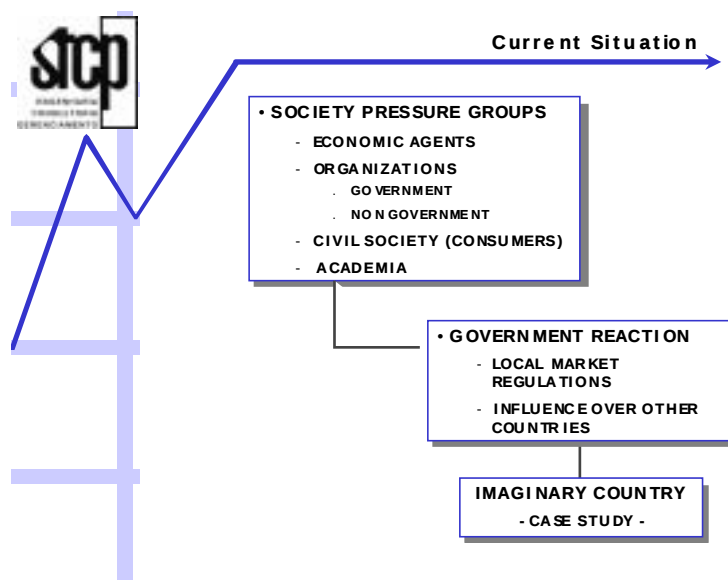
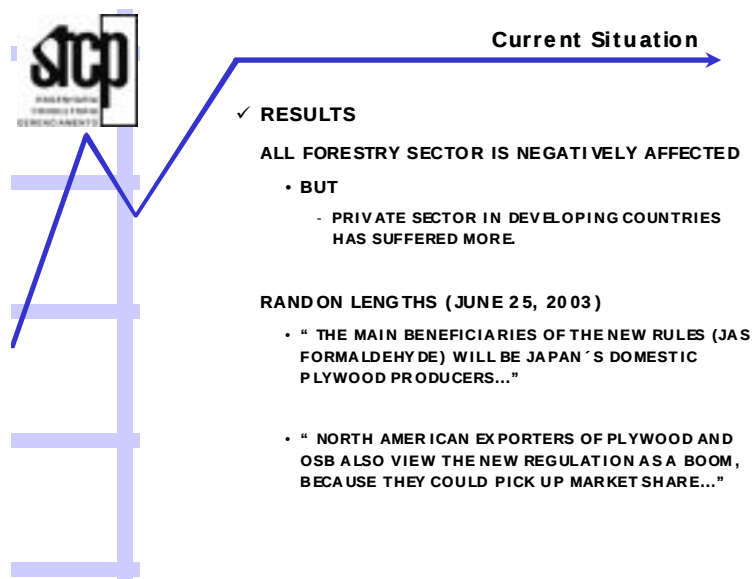
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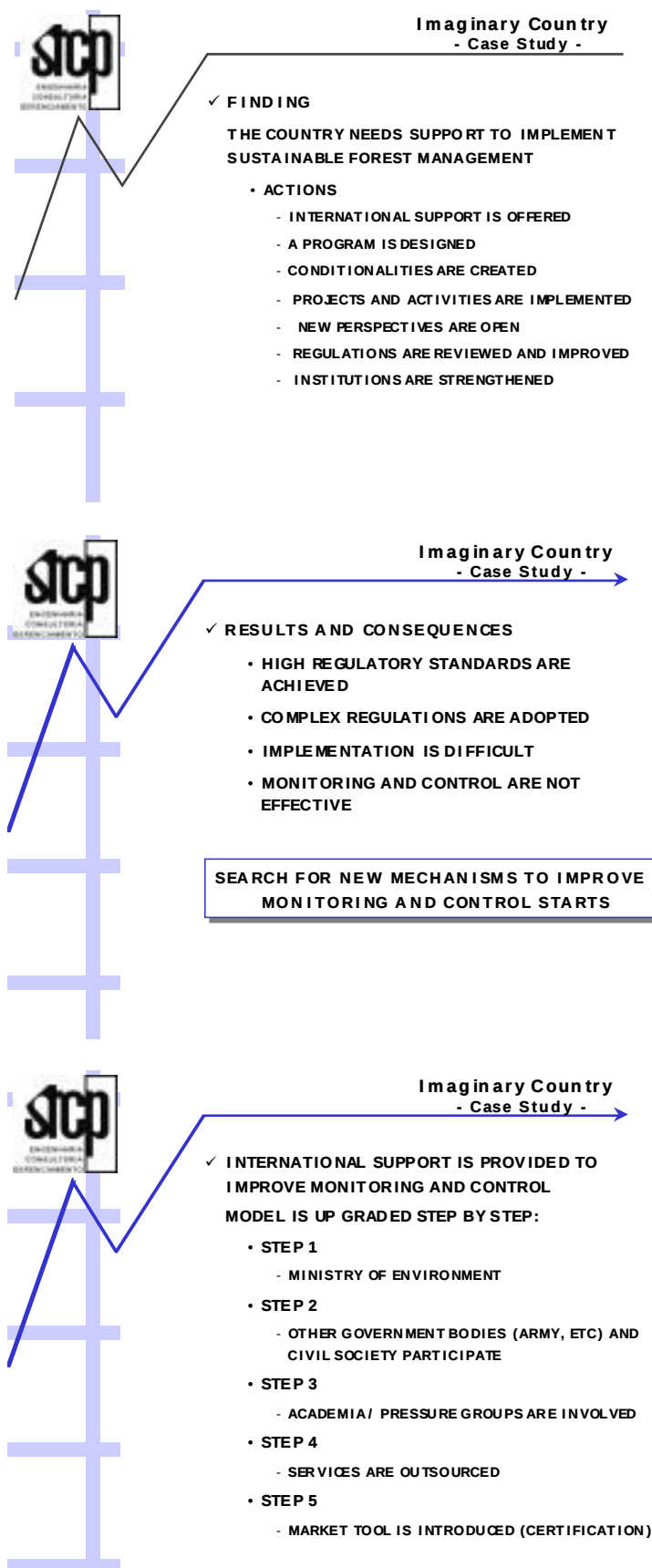


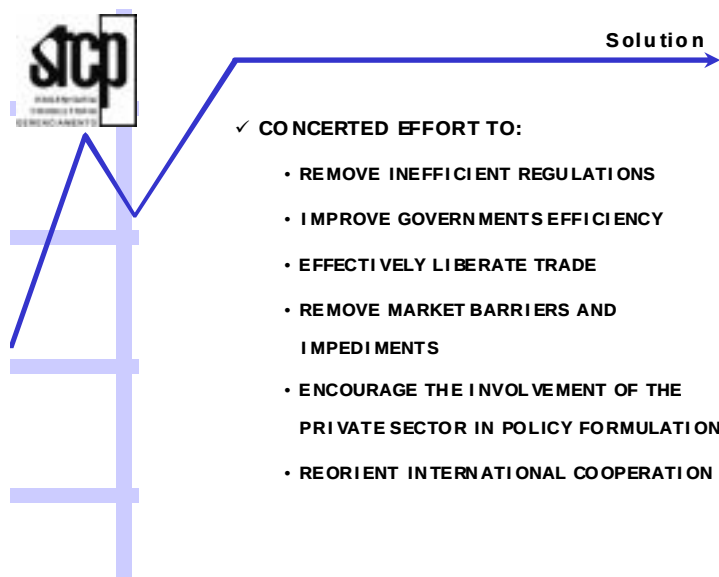
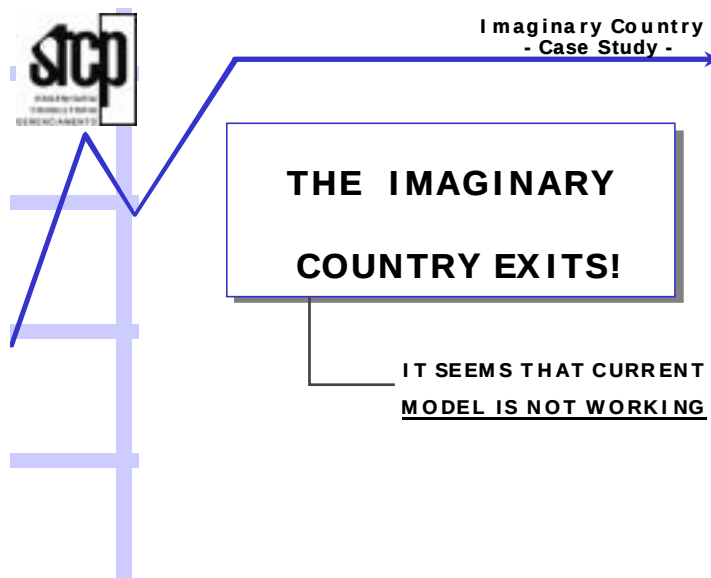
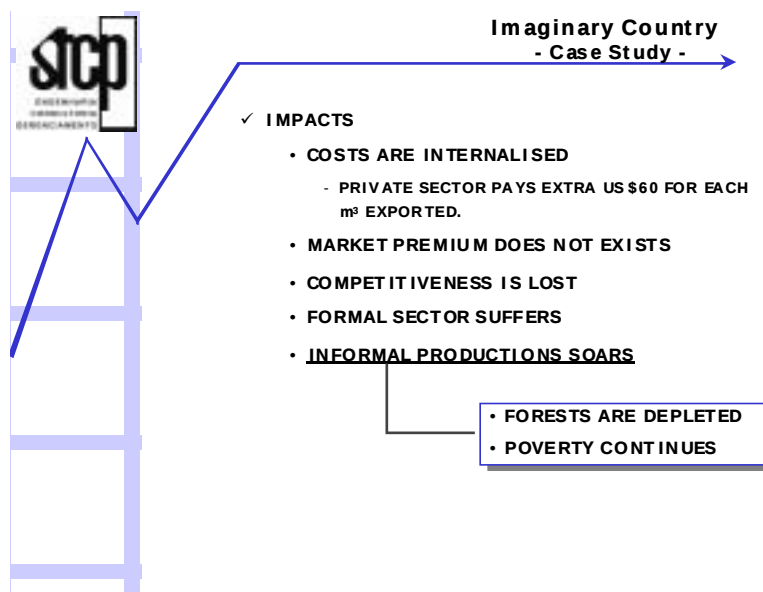
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Discussion:

At the end of the day and given the clarity of this presentation, the discussion was brief, focusing mainly on a reduction of governmental interventions into market development. It was underlined that a code of conduct for forest industries, self-regulation and self-auditing was the objective of the private sector based on common policies with regard to the establishment of forest resources and their management. Competitiveness in the sector would positively influence the approaches to sustainable forest management. On the other hand, it was noted that non-market interventions by governments are actually the basis for saving forests from overexploitation and degeneration through anthropogenic interventions.

With regard to forest plantations and planted forests, it was discussed whether or not SFM is really the concept since plantations do not provide all the products and particularly the services of natural forests. It was mentioned that the forestry community needs to look at “forests” in a different way by integrating natural forests and forest plantations into one concept rather than looking at the forest plantations in isolation. It was noted that particularly tropical forests will not be saved and managed sustainably in the future, if the current model of dichotomy of natural forests versus plantations continues to be applied.

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