The legal basis for verification systems – standard setting for legal compliance
Adrian Wells

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This paper explores the role, content and development of legality standards for verification in the forest sector. It discusses the key principles of standard setting and the questions these pose in terms of scope, content and process. The paper also highlights questions relating to the status of legality standards in standing for applicable laws and regulations, as well as to issuances of certificates of compliance. The paper draws on VERIFOR case studies of forest-sector verification, as well as discussions at the VERIFOR Experts Meeting (Palma de Mallorca 27 – 28 April 2006).

Key concerns
- In defining the scope of a legality standard, how might the balance be struck between legitimacy (incorporating social standards) and its applicability?
- What if there is an insufficient basis in national law for incorporating for social and environmental standards that certain stakeholders may regard as essential?
- To what extent do legality standards risk excluding small-scale producers, e.g. due to the high costs of compliance?
- What are the processes by which a legality standard should be developed, to ensure adequate buy-in and 'policy closure'? Might a focus on legality imply a different kind of process from initiatives to agree C&I for SFM?
- What is the legal status of a legality standard, and who is liable if determinations of compliance with such a standard prove to be inaccurate?

1. A legality standard as a necessary condition for effective verification.

In many countries the legal and regulatory frameworks affecting the forest sector are highly complex. They may provide an unclear basis for audit. In such cases, verification may require prior agreement over a set of unambiguous standards for determining legal compliance.

In practice, a standard for verification of legal compliance implies:
- *Prioritisation* of existing laws and regulations depending on the objective of the verification system and the mandate of the lead institution.
- *Augmenting* regulatory frameworks to incorporate clear Standards of Performance (SOPs).

Standards for verification of legality in the forest sector may vary depending on whether they are intended to serve national interests, bilateral trade agreements, government procurement contracts, or the purposes of private-sector or NGO initiatives.

1.1 National standards-setting processes

A few countries have established mandatory performance standards as the basis for verification of legal compliance, through the development of mandatory Criteria and Indicators (C&I) for Sustainable Forest Management (SFM). In Ecuador, the Ministry of Environment facilitated the development of a simple set of mandatory C&I against which to verify compliance as part of broader reform of the legal and institutional framework governing the sector (see Box 1). Costa Rica developed mandatory C&I for SFM under its National Certification Forestry Commission (CNCF). These were incorporated into forest law by Ministerial Decree, and now provide the basis for monitoring legal compliance by private

forest owners. The Indonesian Ministry of Forests gazetted mandatory C&I as a yardstick for compliance assessments of industrial concessions by government-appointed auditors (LPIs). Following on the heels of the *ITTO Guidelines for the Sustainable Management of Natural Tropical Forests* as well as the rise of SFM certification, Malaysia developed national C&I which now provide the basis for both mandatory public audits as well as third-party certification of State forest administrations and licensees.

Box 1 The development of a legality standard in Ecuador

In Ecuador, the development of standards for verification of legal compliance in the forest sector took place in the context of the 1999 National Strategy for Sustainable Forestry Development. Amongst others, this had the objective of reversing forest loss through SFM. The Strategy emerged through broad stakeholder participation, and set the basis for a comprehensive overhaul of the legal and institutional framework governing the forestry sector. This included the development of an Outsourced Forest Control System (SNTCF). In April 2000, Executive Decree No. 346 introduced important changes to the Regulations of the 1981 Forestry and Conservation Law. It established five basic criteria for sustainable forest management: (i) production sustainability; (ii) maintenance of forest cover; (iii) biodiversity conservation; (iv) private-public co-responsibility in SFM; and (v) reduction of social and environmental impacts. Then in mid-2000, the Minister of Environment issued Decree No. 131 on forestry with the aim of implementing Executive Decree 346. Amongst others, this introduced simplified operational rules for forest management, as well as 32 verifiable indicators for monitoring of forest management activities. These indicators were considered a pre-requisite for implementing the SNTCF.

Source: Guillermo Navarro, Filippo Del Gatto and Martin Schroeder (2006), *The Ecuadorian Outsourced National Forest Control System*, VERIFOR Country Case Study 3 www.verifor.org

(ii) Standards-setting under bilateral trade agreements

Mandatory standard setting for legal compliance is now also being driven by bilateral agreements responding to international processes on Forest Law Enforcement, Governance and Trade (FLEGT), as promoted by the World Bank and the European Union (among others). With a focus on compliance with existing laws and regulations, these initiatives have a more specific set of objectives than standards-setting for SFM. However, they also imply verification of a wider range of activities that most national C&I processes; not just forest management, but also timber processing and trade. An example of one such bilateral agreement is the 2002 UK – Indonesia *Memorandum of Understanding on Cooperation to Improve Forest Law Enforcement and Governance*, which has sought to develop a standard for trade in legal timber (see Box 2).

Box 2 The development of a legality standard under the UK – Indonesian MoU on Forest Law Enforcement and Government

UK – Indonesia *Memorandum of Understanding on Cooperation to Improve Forest Law Enforcement and Governance and to Combat Illegal Logging and the International Trade in Illegally Logged Timber and Wood Products* was signed in April 2002. This mandated the development of a standard for purposes of legal verification, reflecting concerns over the complexity of the existing regulatory framework.

A team to develop the standard was established under the auspices of the Ministry of Forests. This then contracted an Indonesian NGO, Yayasan Madanika, to carry out multi-stakeholder consultations. The draft standard was field-tested by The Nature Conservancy (TNC), under an initiative to pilot a third-party wood legality verification and tracking system in East Kalimantan Province. This included the development of audit guidelines. Following two subsequent rounds of stakeholder consultations, the Indonesian Ecolable Institute (LEI) was asked to take over the legality standard and to facilitate resolution of outstanding differences. Amongst others, LEI is now working to harmonise MoU-TNC standard with the GoI's Timber Administration System (PUHH).

The Indonesian MoU – TNC standard currently consists of 7 Principles and 18 Criterion to guide auditors in verifying compliance with laws and regulations stipulated in the standard. These span a subset of laws and regulations applicable to large scale forest operations undertaken in Indonesia's natural forest that stakeholders involved in the Standard's development considered to be the most relevant. The standard also contains provisions on land tenure and use rights; social environmental impact; community relations and workers rights; timber harvesting laws and regulations; forest taxes; log identification, transfer and delivery; as well as timber processing and shipping.

The development of the MoU – TNC standard has, however, raised complex dilemmas in terms of its coverage of existing national laws and regulations, and the implications this had for both its perceived legitimacy as well as its practicality; with particular debate of the incorporation of provisions requiring the legal gazettement of concession boundaries and the Free and Prior Informed Consent (FPIC) of local communities. The Standard has yet to be official endorsed by the GoI. Whether the Standard should ultimately constitute a mandatory standard or voluntary 'best practice' is still being debated.

More recently, the EC FLEGT Action Plan and Council Regulation 2173/2005 mandated the negotiation of licence agreements for imports of legal timber into the EC. Given the constraints on unilateral mandatory standard setting under WTO-GATT[1] (see Box 3), EC FLEGT policy envisages that each producer country should develop its own definition of legally-produced timber that provides an 'unambiguous, objectively verifiable and operationally workable' standard, that is also amenable to change in light of regulatory reforms.[2] This follows the example of the UK – Indonesia MoU. Processes to define such standards have now been initiated in Cameroon and Ghana. Reliance on national laws for purposes of international trade is, however, problematic given the diversity of national laws, especially in relation to social and environmental concerns where producer-country legislation may also be less clear or even contradictory.

[1] General Agreement on Trade and Tariffs
[2] FLEGT Briefing Paper 9, as developed by the EC Ad Hoc Working Group on FLEGT

Box 3 Constraints on mandatory standard setting for international trade in legal timber

Given that forests remain a sovereign resource under international law, timber-producing countries have fiercely resisted the imposition of mandatory international targets and standards on the sector. International standard setting has been restricted to the development of voluntary guidelines and certification schemes for sustainable forest management (SFM). The imposition by timber importers of mandatory standards for legal compliance may in any case violate WTO rules. Although legality constitutes a process or production method that bears no relation to the physical characteristics of timber products (and so arguably falls outside the remit of the WTO Agreement on Technical Barriers to Trade), it is nevertheless subject to GATT discipline. This includes the requirement for equal treatment of 'like' products. According to the WTO Dispute Panel, distinguishing products on the basis of 'unrelated' process or production methods is allowed under GATT, so long as such a scheme is voluntary (i.e. that products not meeting the standard would continue to gain market access).[3] As such, countries wishing to regulate the legality of imported timber can only look to producer-country legislation as may apply to individual consignments or operators.

(iii) Procurement policy

A number of importing countries are now establishing guidance for government procurement of legal and sustainable timber. Amongst others, guidance issued by the Central Point of Expertise (CPET) for UK Government timber procurement policy states that forest managers should hold legal rights to harvest, and that forest managers and contractors should comply with national law on forest management, the environment, labour and welfare, health and safety, CITES, as well as payment of royalties and taxes. However, precisely because countries' laws may be vague and contradictory, the guidance also states that "*the FLEGT process has proposed that in such countries it will be necessary to have or develop a practical working definition of 'legal' or a set of core laws which must be met which has support from major stakeholder groups. This can be done through a national standard-setting process or other appropriate means*."

(iv) Private-sector and NGO standards initiatives

A number of private-sector and NGO initiatives have also begun to develop their own non-binding standards and protocols on compliance with producer-country laws, with the aim of promoting trade in legal and sustainable timber. These seek to address legality within the framework of a step-wise or phased approach to third-party certification of SFM. This reflects a concern that a focus on legality (as promoted by FLEGT) should not detract attention from the goal of sustainability, but that sustainability is also unattainable at first instance for many forest owners and managers. Initiatives include the WWF – Global Forest Trade Network (WFF – GFTN)'s Responsible Purchasing Programme which progresses forest owners and managers from legal to credibly certified under time-bound action plans.[4] However, given that these initiatives aspire to international certification standards, e.g. as established by the Forest Stewardship Council (FSC), their objectives of sustainability may be more ambitious in their scope that those of national C&I processes. The latter may attempt to simplify standards as a means of facilitating compliance, e.g. by merging criteria as in Ecuador.

[3] Dispute Panel in *Tuna - Dolphin*

[4] White G & Sarshar D, (2004) *Responsible Purchasing of Forest Products, Global Forest & Trade Network WWF*, Gland.

2. Principles applicable to standard setting

Notwithstanding differences in their objectives, experiences including the development of C&I for forest management in Ecuador and Costa Rica and the UK – Indonesia MoU Standard suggest common principles essential to standard setting for purposes of legal verification. These include:

- *Legitimacy* – a standard should enjoy broad stakeholder acceptance as the benchmark for legal compliance.

- *Applicability* – a standard needs to be implementable, without imposing transaction costs that render compliance uneconomic.

- *Specificity* – without clear, measurable Standards of Performance (SoPs), auditing legal compliance can be difficult.

However, meeting these principles raises complex dilemmas over: (i) whether existing legal frameworks provide a viable basis for standard setting without legislative and regulatory reform; (ii) whether a standard should seek to represent all relevant laws and regulations or only a sub-set; and (iii) the process needed for developing, reaching agreement on and implementing a standard.

3. To what extent does standard setting necessitate underlying legal and regulatory reform?

National legal and regulatory frameworks vary in terms of their ability to translate into standards that are both applicable as well as perceived as legitimate by most stakeholders.

3.1 Questions of legitimacy

In many cases, national regulatory frameworks governing the forest sector are weighted in favour of conservation or commercial harvesting and processing; and work to exclude small-scale, often poor, forest managers – either by intent or by mere omission. In Indonesia, Law 41/1999 on Forests classifies as State forest, forest areas that are not already subject to existing rights, i.e. titles issued in accordance with the Basic Agrarian Law (BAL) 1960 by the National Land Agency (BPN). It does not, however, recognise customary rights as detracting from their status as State forest. This reflects the fact that customary lands have mostly never been delineated by government, despite the fact that implementing regulations under the BAL[5] allow for the recognition and registration of customary rights[6]. Furthermore, while the latter provide for registration of private customary rights, land registration systems do not currently accommodate collective claims. As a result, the delineation and allocation of forest lands simply overrides customary rights and land-use systems. Nor do most local community producers possess a legal right to harvest timber within the National Forest Estate. Attempts under the UK – Indonesia MoU to derive a standard from existing laws and regulations, and their focus on compliance by large-scale concessions, have been criticised as legitimising the *status quo* or even reinforcing exclusion of customary land owners and small-scale producers, and concentrating the legal trade in the hands of existing industry cartels.

3.2 Questions of applicability

[5] Government Regulation 24/1997, Ministerial Decree 5/99

[6] A. Contreras-Hermosilla and C Fay (2005) *Strengthening forest management in Indonesia through land tenure reform: Issues and framework action*, Forest Trends, Washington DC pages 8 - 11

In many producer countries, a culture of non-compliance is so embedded that most forest managers would be found illegal if the legal and regulatory frameworks governing the sector were to be fully enforced.[7] The poor in particular face considerable barriers to legal compliance, even where they are accorded rights in forests. This is to do with the complexity of current regulations and the high transaction costs of obtaining permits. In Honduras, these problems have forced members of community-based forest cooperatives into illegally where the economic returns for timber on the domestic market were already slim. High transaction costs also left licensed community logging operations vulnerable to capture by external timber syndicates, who made use of community permits to access resources and 'legalise' production.[8] In both Indonesian Papua and Cameroon, equivalent problems led to the withdrawal of community logging licences without providing communities with an economically viable alternatives.[9] Similarly, in Costa Rica, full compliance with mandatory C&I for SFM leaves managers USD200 in deficit per hectare, necessitating subsidies through Payments for Environmental Services.[10]

3.3 Questions of specificity

Legal and regulatory frameworks are not designed for purposes of audit. Regulatory provisions may not be sufficiently specific to provide unambiguous standards of performance. In British Columbia, for example, environmental groups have criticised the introduction of 'results-based' legislation (the Forest and Range Practices Act – FRPA) which replaces a more prescriptive Act, the Forest Practices Code. There is intense debate about whether the new law is sufficiently specific for compliance auditing to assure the achievement of sustainable forest management, which is the policy goal advocated by both government and civil society. Discussions are currently taking place about the need to develop specific indicators to be used to assess compliance with the new results-based Forest Act.[11]

The specificity of standards with respect to disputes over land and local community rights can be especially problematic. Indonesia, efforts to field-test the UK – Indonesia MoU standard highlighted insufficient guidance on what auditors should be looking for in relation to provisions for the gazettement of concession boundaries. Similarly, while Criteria 2 and 3 of the Malaysian C&I for SFM (MC&I 2002) require the assessment and documentation of disputes with local communities, as well as 'appropriate mechanisms' for dispute resolution, some stakeholders have argued that related indicators and means of assessing compliance may not be sufficiently specific or performance based.[12]

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[7] N. Bird, T. Fometé and G. Birikorang (2006*), Ghana's Experience in Timber Verification System Design*, VERIFOR Country Case Studywww.verifor.org, page 6

[8] Wells, A., F. Del Gatto, M. Richards, D. Pommier and A. Contreras-Hermosilla (2004) *Rural livelihoods, forest law and the illegal timber trade in Honduras and Nicaragua*. A case study for CIFOR/PROFOR: "Forest Law Enforcement and Rural Livelihoods" study (in press)

[9] DFID – Multi-stakeholder Forestry Programme (2006) *Whose rule of law? Forest law enforcement and community logging rights in Indonesian Papua* (in press); presentation of Cameroon case study, Timotheé Fometé, VERIFOR Expert's Meeting, 27 – 28 April 2006.

[10] *Pers. comm.*, G. Navarro, CATIE, VERIFOR Experts' Meeting 27 – 28 April 2006.

[11] Schreckenberg, K. (2006) *Verification in the Forest Sector of British Columbia*, Canada, VERIFOR Country case study 2. Pages 5 - 6

[12] Wong Meng Chuo, *A Report on the Malaysian Timber Certification Scheme*, FERN Sept. 2003.

4. The scope and ambition of a standard – reconciling legitimacy with applicability.

4.1 The components of a legality standard

While the development of a legitimate and workable standard may depend on regulatory reform, it also depends on the scope and ambition of a standard – in particular whether a standard should represent all relevant laws and regulations or merely a 'critical sub-set'. If the latter, is it possible to have 'partial legality'?

This is perhaps the most complex and contested area of standard setting for legality, in a sector which is typically heavily regulated with hundreds of laws, implementing regulations and administrative measures. Depending on national context, a legality standard for the forest sector might include some or all of the following components:

- *Legal origin* defined as simply as legal right to harvest, or as also including prior determination and settlement of tenurial claims, legal gazettement of concession boundaries, as well as the Free and Prior Informed Consent (FPIC) of local communities with respect to cutting operations on community lands;
- *Legal harvesting* including compliance with permit conditions, payment of royalties, forest management regulations including mandatory C&I for SFM, as well as laws on environment, labour and welfare and health and safety;
- *Legal processing* including compliance with domestic processing quotas, guarantees against mixing with non-legal sources, and payment of processing levies;
- *Legal trade and export* including export licensing, procurement of necessary CITES authorisation and customs clearance.

Legal standards may not consist of all of these components, depending on the objectives of verification. E.g. in Ecuador, the standard for compliance under the SNTCF did not include processing.

4.2 The dilemmas of prioritising laws and regulations for inclusion in a standard

Different interest groups compete to incorporate or exclude specific laws and regulations from the scope of a standard. This makes prioritisation a highly contentious issue, in terms of:

- Whose rights are subordinated through exclusion, with implications for perceived legitimacy?
- Who bears the transaction costs of inclusion, with implications for the workability of a standard?

The development of the UK – Indonesia MoU standard (see Box 2) illustrates these dilemmas. A number of NGO and private-sector trade-based initiatives argued that a legality standard that adopts an expansive interpretation of national laws may be inoperable in situations of weak government, and even work to exclude the majority of forest owners and managers. Efforts to pilot the Indonesian standard led assessors to conclude that the standard was 'socially heavy', making it difficult and costly to verify. Of particular concern were requirements to: secure the Free and Prior Informed Consent (FPIC) of local communities, and also legally gazette concession boundaries. In a situation where only 10% of the National Forest Estate has been fully gazetted in line with stipulated procedures (including notification of local communities),[13] these requirements present a significant challenge for existing licence holders.

The difficulty of achieving and auditing legal compliance as envisaged by the Indonesian MoU – TNC standard prompted a handful of NGO – Private Sector initiatives to adopt a

[13] A. Contreras-Hermosilla and Chip C Fay (2005) *Strengthening forest management in Indonesia through land tenure reform: Issues and framework action*, Forest Trends, Washington DC, page 13.

simpler definition of legality - at least as an entry point to achieving SFM. This includes the Tropical Forest Foundation (TFF) which has adopted a subset of the requirements set out in the Indonesian standard. The TFF standard emphasises forest management, including criterion on chain-of-custody. While it contains provisions on community development, it also excludes requirements for Free and Prior Informed Consent (FPIC), as well as community involvement in the gazettement of concession boundaries. Nevertheless, indigenous rights groups regard legal boundary gazettement and FPIC as the minimum necessary to address the grievances of customary groups whose rights have been overridden by forest land allocation and delineation.

Similar problems have arisen in Ecuador (see Box 1). While standards for legal compliance under the Outsource Forest Control System (SNTCF) were initially limited to forest management, one of main arguments of industry against the system (leading to its suspension in 2003) was that the SNTCF only targeted legal operators, while excluding illegal deforestation and land-use change from its purview. Dialogue to re-establish the verification system has now tried to include land use under a new, decentralised mechanism, but this has serious implications in terms of institutional capacity and the cost of enforcement.[14]

Difficulties over prioritising which laws and regulations to include in a standard may be partly addressed by: (i) measures to phase-in a standard; (ii) placing duties on the State as well as on forest managers; and (iii) differentiating compliance measures; (iv) tackling areas of over-regulation and high transaction costs; and, (v) seeking clarity over the objectives of verification.

4.3 Phasing in a standard

A number of private-sector and NGO initiatives have begun to develop their own voluntary standards and protocols on compliance with producer-country laws, with the aim of promoting trade in legal and sustainable timber. These seek to address legality within the framework of a step-wise or phased approach aiming at SFM certification. Initiatives include the WWF – Global Forest Trade Network (WFF – GFTN), as well as the Keurhout Protocol for Validation of Legal Claims. The latter adopts a simple definition of legality as the first in a three-step process towards SFM certification (see Box 4). The logic behind a step-wise approach is that 'legal' should not detract from the goal of 'sustainable' and should not at the same time present such a formidable hurdle as to render legality impossible to achieve. The approach attempts to reconcile legitimacy with workability. The implication would be to adopt a simple definition of legality and to then gradually "raise the bar" against clearly defined targets.

Box 4 – Step-wise approaches to legality

The Protocol for Validation of Legal Claims, as developed by the Dutch standards institute Keurhout in association with the Netherlands Timber Trade Association (NTTA)[15] "lowers the bar" on legal compliance, but as part of a three-step process towards SFM certification. The first step relates to Legal Origin, including whether timber has been harvested in compliance with laws and regulations in the country of origin governing permits, respecting protected areas, species, tree dimensions and harvest volumes. The second step requires compliance with all other relevant laws and regulations pertaining for forest management including labour and environmental standards. Timber that complies with legal origin, as well

[14] *Pers. comm*.. H. Thiel 31-05-06

[15] Kerhout's Protocol for Validation of Legal Claims enables assessment of the content and reliability of written claims to Legal Origin as issued by a third party with respect to five aspects: (i) legal registration of logging company, (ii) lawful permit for logging; (iii) acceptance/ recognition of customary cutting rights; (iv) selection process of trees to be cut; (v) monitoring and corrective actions.

as the second level of legal compliance is considered "transition timber" moving towards SFM certification – the third step and the highest level of management performance. "Transition" licence holders are expected to enter into a third-party verified programme for progressive realisation of SFM standards against agreed time-bound targets.[16]

A similar approach has been adopted by SGS's Independent Validation of Legal Timber (IVLT). This distinguishes Verification of Legal Origin (VLO), focusing on production rights, legality of ownership and tax payments, from Verification of Legal Compliance (VLC) with respect to forest management planning and exploitation. Under this system, rules on VLO and VLC can be progressively tightened enabling continuous improvement over time.

Proforest's Modular Implementation and Verification System (MIV) has also been designed to support phased approaches to certification and has been adopted by schemes such as WWF-GFTN. The MIV System distinguishes three levels of legality, spanning:

- *resource rights* - legal rights to harvest; protection of the legal and customary rights of local people; and that applicable fees, royalties and taxes have been paid;
- *operating legally* - compliance with all relevant local, national and international laws and regulations on environment, tenure, indigenous and workers rights, community development, health and safety, trade etc; as well as a system for tracking changing in legal requirements and compliance;
- *control of unauthorised activities* – including identifying possible threats, developing systems for prevention and control with other stakeholders, and monitoring the success of control activities.[17]

NGO – private-sector initiatives may attempt to reconcile pragmatism with legitimacy, but such step-wise approaches by have nevertheless attracted controversy by:

- assuming that there can be agreement over a definition of full legal compliance, when this end-point is itself heavily contested in some national contexts; and,
- attempting to address the issue of 'legality' themselves when determinations of legal compliance remain a sovereign matter.

Step-wise approaches could be adopted for mandatory-standard setting by national governments. This implies rigorous auditing to secure incremental improvements in compliance across the board, and a careful balance of managed compliance (such as corrective action requests) with adequate penalties for failure to achieve performance targets.

Step-wise approaches are, however, fundamentally problematic in presenting short-term proxies for legality (such as 'legal origin') that add up to less than what producer-country laws and regulations require.

4.4 Placing duties on the State as well as on forest users?

Tensions between "lowering" and "raising" the bar for legal compliance in Indonesia partly reflect lack of clarity over whether a verification system should secure compliance merely by licensees but also by the State. Amongst others things, negotiated land allocation and settlement of forest boundaries with local communities arguably constitute a constitutional and statutory obligation of the State, rather than a duty that can be imposed on concessionaires. So concerns within the private sector over the applicability of a standard may be partly addressed if it were to bind not simply on licensees but also on producer-country

[16] Institution Support and Analaysis, Forests and Landuse (ISAFOR) (2005) Introduction to the legal timber issue and the Kerhout Protocol for Validation of Legal Claims.
[17] Nussbaum, R., I. Gray, S. Hickman, (2003) *Modular Implementation and Verification System (MIV); a toolkit for phased application of forest management standards and certification*, Proforest.

governments. While standards for boundary gazettement and FPIC may be onerous for licence holders, they are in large part the responsibility of forestry administrations.

The fact that only a small proportion of the Indonesian National Forest Estate has been legally gazetted reflects a failure on the part of government that should not necessarily be passed on to licence holders to resolve. Similar arguments could be made in Malaysia where recent rulings of the Court of the Appeal affirm a fiduciary duty on government to gazette aboriginal lands and to put in place measures for payment of reasonable compensation where such land may be taken for other purposes (arguably, including logging). The issue, therefore, is not whether such requirements should or should not be incorporated into a legality standard. Rather, it is one of ensuring that obligations for delivery against elements of a legality standard are clearly allocated between licensees and the State.

Similarly, if a standard is to secure compliance by State administrations as well as forest users, then it cannot function in isolation of broader guarantees on public accountability. This includes statutory rights on access to information and participation, public complaints mechanisms (ombudsmen – an effective agent in PNG) and legal empowerment (in Malaysia, for example, the lack of legal aid potentially constrains recourse to the courts by local communities to resolve boundary disputes).

4.5 Focusing on compliance measures rather than scope

One further option in enhancing the workability of a legality standard without necessarily restricting its scope might be to focus on the type of *compliance measure*.

Depending on the performance criteria, distinctions could be made between those offences that trigger compliance enforcement (e.g. an administrative sanction and/or prosecution), and those that trigger compliance management (e.g. corrective action requests). This is the approach taken by Sabah's 100-year SFMLAs, which seek to gradually close the gap on legality through routine audits and capacity building.[18]

Ecuador also enhanced the applicability of its standards for legal compliance by making adjustments to compliance measures. In this case, the SNTCF favoured administrative measures (fines and seizures) over criminal proceedings with respect to illegal harvesting and trade. This was justified on grounds of alleged weaknesses in the country's judiciary system which offers little, if any, guarantee of forest crime prosecution.[19]

4.6 Tackling areas high transaction costs of compliance

The development of the Outsourced Forest Control System (SNTCF) in Ecuador attempted to address these concerns that verification could work to the detriment of small-scale forest producers by incorporating measures to reduce the transaction costs of legal compliance. This included efforts to bring administrative services directly to communities, simplified operational rules for SFM, tax exemptions on permits for extraction of certain timber species from agroforestry systems and minimal bureaucracy for extraction of planted timber. In addition, reforms to the legal and regulatory framework introduced opportunities to prove land tenure through a certificate that shows that the land title is in process or through an oath

[18] Wells, A. (2006) *Systems for Verification of Legality in the Forest Sector, Malaysia*. VERIFOR country case study www.verifor.org

[19] G. Navarro, F. Del Gatto and M. Schroeder (2006), *The Ecuadorian Outsourced National Forest Control System,* VERIFOR Country Case Study 3 www.verifor.org

declaration with three witnesses that attests possession of the land; this allowed poor forest holders without an official land title to obtain logging permits.[20]

The development of a legality standard could, however, exacerbate the transaction costs of compliance by placing a 'premium' on administrative requirements necessary for legal validation of exports. Under conditions of weak public governance this might create opportunities for rent-seeking if effective public oversight and complaints mechanisms are not also put in place.[21]

4.8 The need to clarify objectives

Phasing-in a standard, sharing liability with the State, differentiating compliance measure and tackling the transaction costs of compliance may all work to enhance a standard's applicability. Whether a standard can be both applicable as well as legitimate is, however, ultimately rooted in the ability to agree the objectives of verification. Ecuador agreed the objectives of verification as part of a comprehensive overhaul of the forest sector. The overhaul included a new National Strategy for Sustainable Forestry Development, as well as comprehensive legal and regulatory reform. This arguably allowed stakeholders greater space to position and resolve contentious issues. Some Indonesian stakeholders take a similar position. They argue that, with a legal and regulatory framework in such dispute, a legal standard for verification cannot be agreed without a similar overhaul of the sector including multi-stakeholder agreement over SFM norms.[22] National standards-setting processes can, however, be highly time-consuming. Debates over the Malaysian C&I still continue some ten years after the process began. Ecuador, too, struggled to maintain consensus over the scope of its verification system, with pressure to ultimately include illegal land conversion and land-use change within the scope of its standard despite shortages in institutional capacity to enforce it.

The difficult of agreeing objectives is further complicated by the requirements of bilateral trade agreements on legality, government procurement policies, as well as NGO and private-sector timber certification processes. Amongst others, Briefing Paper 9 of the EC Ad Hoc Working Group on FLEGT emphasises that legality is only a stepping-stone to SFM, the logic being that legality is as a necessary precondition for SFM and simpler to achieve in the short term. Yet concepts of sustainability differ. The international discourse on FLEGT tends to promote standards equivalent to third-party certification schemes such as FSC. National C&I processes may adopt a narrower focus. Standards-setting under the auspices of the Ministry of Environment in Ecuador was highly selective in choosing criteria, sometimes merging two or three into one. It also excluded both illegal land-use change and processing (the latter was seen as less of problem with respect to illegality).[23] Producer-country's objectives in standard setting may not, therefore, address the concerns of northern consumers in respect of licensing agreements under FLEGT. In the absence of mandatory standard setting by the EU, this has raised concerns over "shifting goalposts" in some producer countries.[24]

In view of this complexity, one lesson that might be drawn from existing national and bilateral standard-setting processes is that (in some contexts) the stated objectives of verification should perhaps be pared down to something less ambitious than either "legal" or

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[20] G. Navarro, F. Del Gatto and M. Schroeder (2006), *The Ecuadorian Outsourced National Forest Control System,* VERIFOR Country Case Study 3 www.verifor.org

[21] *Pers. comm*, A. Bohanic, VERIFOR Expert's Meeting, 27 – 28 April 2006.

[22] *Pers. Comm*, Ngadiono, VERIFOR Expert's Meeting, 27 – 28 April 2006.

[23] *Pers. comm*, H. Thiel, VERIFOR Expert's Meeting, 27 – 28 April 2006.

[24] Timber producers in Malaysia, for example, question whether a nationally-defined legality standard will in fact increase security of access to European markets or merely succumb to "shifting goalposts" depending on European consumer pressure. In particular they refer to previous efforts to establish standards for SFM under a programme of collaboration with the Dutch standards institute Kerhout, which failed to secure the acceptance of Dutch NGOs.

"sustainable"- for example, it might be enough to show only that timber has not been stolen. This could allow consensus to be reached around a more specific standard, the objectives of which could be revisited at a later date.

5. By what process should a standard be defined?

National standard-setting processes inevitable provide space to contest norms, the more so with an explicit focus on a "definition of legal". This creates very strong pressure for stakeholder inclusion in standards-setting processes, and some parties may perceive the process as an opportunity to promote legal reform where there may otherwise be limited opportunity to position their interests. A focus on legality therefore implies a process that is likely to be more politicised and heavily contested than multi-stakeholder processes for agreement on C&I for SFM.

While broad participation is essential in securing broad acceptance of a standard, the experience of the UK – Indonesia MoU (see Box 2) demonstrates how difficult it is to put boundaries round the process. The development of the standard created the space for civil society and NGOs to raise objections to Indonesia's legal framework, i.e. that the current legal framework subordinates local people and does not recognize the rights of customary communities to forest resources. Other interests groups also pushed the inclusion of laws and regulations relating to forest management, regulations related to mill capacity (a major driver of illegal logging). But as a consequence, the process became caught between:

- Those concerned to deliver a simple, auditable and cost-effective standard as quickly as possible (the implication being solutions were to be found within the current legal framework); and,
- Those who saw the standard as an opportunity to address fundamental injustices in the current legal framework.

The institutional mechanism for developing a legality standard would need to be able to resolve such differences. Despite the fact that the MoU – TNC standard created vital space for debate, many Indonesian stakeholders saw the standard as a northern-driven initiative. Through much of its development, the Ministry of Forests had shown limited support and it is not certain whether it will adopt the standard for a Voluntary Partnership Agreement with the EU in its current form. In this respect, the process might have been more effective were it to have been managed from the start by a technically credible Indonesian organization, with the ability to mediate between different interests. Some progress has been made is this respect after the the Indonesian Ecolabel Institute (LEI) has been asked to take over the legality standard. LEI is now working to harmonise MoU-TNC standard with TFF standard and GoI's Timber Administration System (PUHH), with primarily Indonesian representatives. The latter in particular may work to secure Ministry of Forests buy-in. Some stakeholders are optimistic that LEI will be able to build consensus on the legality standard. Others, however, fear that LEI will bring even more stakeholders into an already complicated and messy process.

Indeed in a way different to the development of technical C&I for SFM, the process of determining a legality standard requires oversight by an institution, with the legal and political mandate to end debate and reach "policy closure". While LEI may be working to refine the MoU – TNC standard under the auspices of the Ministry of Forests, it is questionable whether the Ministry of Forests alone has the mandate to provide this kind of political oversight.

The MoU – TNC examples raises the need for more understanding of how legal formulation and reform works in different national contexts. This includes focusing on:

- The key drivers, including the political mandate for verification (e.g. governance, growth), reformist administrators or legislators, CSOs, the Supreme Court etc.

- The political mandate for the process, including executive or legislative supervision with the power to bring "policy closure" (e.g. Ministry of Environment in Ecuador).
- The technical credibility of lead institutions, e.g. the National Commission for Forest Certification in Costa Rica which comprises of national universities, technical NGOs and research centres.
- Alternative channels (technocratic design, judicial interpretation, political negotiation) depending on political culture and legal systems.

There is a risk that demand-side pressure for a legal standard could override or undermine existing national processes and reforms efforts (e.g. by taking the focus off C&I). There is an underlying concern that the process for developing a legal standard genuinely builds existing national processes, including civil society advocacy strategies.

Before the Indonesian standard was taken on by LEI, the UK – Indonesia MoU and TNC faced considerable difficulties in facilitating and reconciling competing pressures on the scope and content of the standard and this raised questions over national ownership of the process. In Cameroon, it is unclear whether a technocratic, donor-driven process housed within Ministry of Forests, has the capacity to address and reconcile competing demands and perceptions without recognising the role of civil society networks in facilitating, mediating the development of the standard. In both countries, questions have been raised over the legality of administrative decision-making (e.g. Ministerial decisions withdrawing small-scale cutting licences). The processes as designed are not necessarily mandated to address and resolve these questions. The later may perhaps be an appropriate subject for Judicial Review.

6. What is the legal status of a mandatory standard?

While a legality standard may constitute a benchmark for legal compliance, what would be its legal status? Participants at the VERIFOR experts' meeting in Palma de Mallorca (27 – 28 April 2006) highlighted four sets of issues in this respect, and that require further analysis in the context of both national and bilateral (FLEGT) processes: (i) the requirement to gazette a legality standard; (ii) the need to determine whether a standard does represent applicable laws and regulations in line with the stated objectives of verification; (iii) the mandate to issue certificates of legal compliance; and (iii) liability where determinations of compliance prove to be false or inadequate.

6.1 The requirement to gazette a legality standard

The authority to gazette a legal standard may depend on the political mandate under it has been developed, e.g. C&I for forest management, facilitated under the auspices of the Ministry of the Environment in Ecuador, which were issued by Ministerial Decree. Depending on the agreed objectives for verification, its scope may include other sectors (e.g. labour, land) which case it may be more appropriate to gazette a standard by Prime Ministerial or Presidential Decree.[25]

6.2 Determination of whether a standard does stand for applicable laws and regulations

Legal gazettement of a standard would in turn require an authoritative determination as to whether a standard constitutes a proper representation of applicable laws and regulations; with a bearing on whether certificates of compliance can vouch for 'legality' or mere 'compliance with a standard'. Authority may not necessarily rest with an individual Ministry,

[25] *Pers. comm.* S. Nguiffo, CED, VERIFOR Expert's Meeting, 27 – 28 April 2006.

but rather with the Attorney General or Ministry of Justice. T the Judiciary may be involved where the validity and interpretation of laws and implementing regulations as incorporated into a standard is contested. [26]

6.3 Issuance of certificates of legal compliance

Producer country governments may choose to outsource assessments of compliance against a mandatory standard to independent third parties though, the issuing of certificates may necessarily rest with a government agency unless an accreditation system is established with a national standards agency.[27] One Ministry could take responsibility for issuing certificates, but where compliance also depends on fulfilment of administrative procedures in respect of other Ministries, e.g. payment of taxes to the Revenue Department of Ministry of Finance, mechanisms may be needed to establish proof of compliance in respect of these other sectors as well. [28]

6.4 Liability

Under a scheme for licensing of legal exports, a producer country would normally not be liable in respect of losses such as demurrage if exporting companies failed to obtained a certificate of legal compliance. Would, however, a producer country be liable if it was established that its determination of legal compliance proved to be inaccurate? A third-party verifier may well be liable under such circumstances, so what of government agencies responsable for issuing legality certificates? To what extent would they enjoy immunity? This requires further analysis.

7. Conclusion

In all cases, a legality standard will need to enjoy broad buy-in, as well as be sufficiently applicable and specific to enable effective verification. This, however, implies complex trade-offs in determining the scope of a standard.

The need to prioritise laws and regulations for inclusion in a standard may be especially contentious as it implies subordination of rights and/or increased transaction costs on the part of some parties. Furthermore, underlying laws may be so contested as to render agreement on a standard unlikely without radical legal and institutional reform. A legality standard could, for example, set out to 'catch the big crooks' but end up criminalising small-scale forest managers if it does not work to re-regulate the sector in ways that facilitate compliance.

Options for enhancing the applicability of a standard without compromising its scope may be to: (i) phase its introduction; (ii) ensure that a standard binds on both forest users as well as on the State (amongst others, so that State responsibilities including the gazettement of concession boundaries are not passed on to licensees); (iii) differentiating between compliance management and enforcement in respect of different performance criteria; and (iv) reducing the costs of compliance by tackling areas of over-regulation and putting in place safeguards against administrative rent-seeking.

Resolving conflict over the scope and content of a standard is, however, ultimately dependent on the ability to agree the objectives of verification. Agreeing on objectives can be extremely difficult where the existing legal framework is disputed, such as in Indonesia. It may depend on a broader strategic overhaul of the sector, as in Ecuador. In some cases, objectives may

[26] *Pers. comm*.. S. Nguiffo, CED, VERIFOR Expert's Meeting, 27 – 28 April 2006.
[27] This raises questions over whether third-party auditors (e.g. Smartwood, SGS) can issue certificates of 'legality' unless it was made explicit that the standard used was entirely voluntary.

[28] *Pers. comm*., S. Nguiffo, CED, VERIFOR Expert's Meeting, 27 – 28 April 2006.

need to be narrower in ambition than ‘legality’ or ‘sustainability’ where these concepts are the source of major differences in understanding.

Briefing Paper 9 of EC Ad Hoc Working Group on FLEGT suggests that a legality standard can be achieved by stakeholder consensus. However, while the development of a legality standard may create the space for vigorous stakeholder debate, it is by no means guaranteed to resolve differences – especially where the underlying legal framework is heavily disputed. Experience in Indonesia and elsewhere suggests standard setting depends on both leadership of the process by a technically competent organisation with strong legitimacy, as well as oversight by an institution with the legal and political mandate to end debate and reach “policy closure”.

The gazettement of a standard, as well as an authoritative determination as to whether it stands for applicable laws and regulations, are essential if certificates issued against it are to vouch for ‘legality’ as opposed to mere ‘compliance with the standard’. These should be anticipated in the process of developing a standard, including sufficient involvement of the justice sector from the outset. Finally, more work is needed on the liabilities that producer countries may incur in respect of legal validation of exports.