



Logging and trade of acquired timber

Legal regulation, procedures and ways to evade them

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Foreword

Globally the problems caused by illegal activities involving timber are becoming more and more topical. At present, this is recognised as one of the causes for the degradation of forests. However, illegal activities threaten not only biologically diverse forests, but also the means of subsistence of local society. They diminish the power of law and cause substantial losses to nations in the form of uncollected taxes and other payments.

Year after year in Latvia, volumes of felled timber and timber export are increasing. Data from the Central Statistics Bureau shows that in 2002, as in the previous years, timber and timber products took up the most significant place in Latvia's export. In comparison with other product groups, the export of timber and timber products showed the largest growth in 2002. Export volumes have increased most rapidly for the largest companies. Taking into account the volume of export and its potential, Latvia's reputation in the international market as a country that exports timber and timber products is becoming ever more important. That's why the reduction of timber of an illegal origin is an important issue both for the sector and for the Latvian nation as a whole.

Several international processes testify that the international community, nations and organisations are acting to reduce volumes of illegal timber:

- Since 1996, the Environmental Investigation Agency (EIA) supports the global strategy that provides for "highlighting" and combating the felling and trade of illegal timber.
- The United Nations Intergovernmental Panel on Forests (IPF) which completed its work in 1997, "invited countries to provide an assessment and share relevant information on the nature and extent of illegal trade of forest products and consider measures to counter such illegal trade." The IPF's successor – Intergovernmental Forum on Forests (IFF) included the "...review of issues that are related to market transparency, as well as illegal trade of timber and other forest products".
- In the May 1998 meeting of G-8 countries an action programme for the forest sector, "Action Programme on Forests" was adopted that comprised commitments to the fight against illegal logging and trade. At this meeting, the states agreed that "Illegal logging robs national governments, forest owners and local communities of significant revenues and benefits, damages forest ecosystems, distorts timber markets and forest resource assessments and acts as a disincentive to sustainable forest management". One of programme's measures was the assessment of internal measures and means of the states, for example, resource acquisition/purchase policy, in order to control the sale of illegal timber and illegally acquired timber on the international market'.
- The Bali declaration was adopted at the international conference in 2001 in Bali: "Immediate action should be taken in order to improve achievements at national level and to strengthen bilateral, regional and multilateral cooperation in the area of violations of forest legislation and forest crimes, especially in the area of illegal timber, comprising illegal commerce and corruption and its negative impact on compliance with laws".
- The issues of the acquisition of illegal timber, its causes, consequences and possible solutions are being investigated in several countries across the world with the support of the World Wildlife Fund and the World Bank Alliance.
- The European Commission organised an international seminar in April 2002 in order to introduce the FLEGT (Forest Law Enforcement, Governance and Trade) process. Representatives from EU member states, from countries that are the largest timber importers and harvesters, companies from the forest industry and NGO's took part in the seminar. In order to promote the fight against the harvesting, processing and trade of illegal timber and timber products, the FLEGT process includes discussions and co-operation between developed countries and new countries that have just emerged onto the international market and produce or consume/import timber or timber products. This also includes the assessment of legislation and reforms in timber acquiring countries, the considerations of governments, for example, considerations related to management, capacity, production capacity, improved realization, as well as trade considerations for commerce for special market access.

Illegal forest exploitation and timber trade cover various forms and take place in different stages of the 'chain' starting from the issue of a felling license up to producers and importers. This question should be considered in a complex form, because illegal operations in the forest industry comprise:

- Illegal activity at the pre-logging stage;
- Illegal logging;
- Illegal timber transportation and trade both in local and international markets;
- Illegal processing of timber (without license, processing illegally felled timber, violating labour legislation) etc.

In accordance with a definition drafted at the Forest Forum of the World Bank and companies from the timber sector, *WB CEO Forum on Forest*, illegal forest exploitation is:

- Felling outside the borders of a determined area or exceeding its limits;
- Exceeding the amount stated in the felling license;
- Any acquisition of timber in the areas determined by the state or municipality as protected and where in accordance with management regulations the acquisition of timber is not permitted;
- Felling without the permission of the responsible authority (inc. the owner of forest) or with falsification of such permission;
- Felling that is not performed in accordance with the forest management plan;
- If trees species, that are recognised as protected at national and international level, are cut;
- The felling of trees, which have died back because of wrong management or natural causes (sanitation cuttings)
- Cutting of trees that have not reached the permitted age or diameter that has been performed by falsifying the results of a forest inventory;
- Concealment of the real volume of felling with the aim of legalise illegally acquired timber and/or to gain the cash with activities that are not recorded in bookkeeping;
- If a felling license is obtained by means of a bribe or using other illegal indemnity;
- Presenting reduced timber value, reduced timber volume, reduced rates of interest etc. in official documentation, as well as concurrently performing activities not corresponding to book-keeping and accounting norms;
- If the felling is taking place, using techniques, working instruments, technology etc. that do not correspond to the requirements determined by the state, as well as violating the rights of employees and not observing rules of labour safety;
- Any other timber felling or action related to timber felling that breaches prohibitions of laws, regulations and other regulating documents;

Illegal trade and/or transportation of timber:

- Export/import of individual tree species that is prohibited by national and international legislation, for instance, in the Convention on International Trade in Endangered Species of Fauna and Flora (CITES);
- Export/import of species of trees without necessary licenses that are on the CITES list;
- Export/import of timber or other timber products breaching national prohibitions;
- Prohibited transportation of timber across the border of a region or state;
- Transportation of illegally felled timber from a felling site to a further place of trade;
- Existing volume of exportable timber exceeds the volume determined in documents;

Illegal processing of timber:

- Timber processing without documentation (if such is necessary in accordance with the law) that verifies its legal origin;
- Activity without processing license;
- Activity without other necessary licenses and permissions (for example, permissions of blasting waste water, accumulation/ gathering of effluent);
- Non-execution of requirements determined in licenses and permissions, also lack of pollution control standards);

The **aim of this research** is to determine all possible stages in the chain “*pre-logging stage – timber trade*” where activities not corresponding to legal regulations can take place, which result in promoting illegal activities involving timber in Latvia.

Within the scope of this research, activities in the areas of timber harvesting and wood processing are examined in the following aspects:

- a) legal regulation;
- b) control arrangements;
- c) “gaps” in the legal regulation and examination of possible violations;
- d) responsibility of non-observing/ violation of legal regulation;
- e) recommendations.

Investigations into timber export, import and transit procedures and action not corresponding to legal regulations in these procedures are outside the scope of the given research.

The results of the research testify that the illegal activities must be considered in the context of the overall “*pre-logging stage – timber trade*” chain. In order to reduce illegal activity during all stages of timber acquisition and realization, legislators, institutions, public organisations and law-enforcement authorities must act uniformly and in harmony, perfecting not only legal regulations, but also Control mechanisms (see recommendations, summary).

The tax and finance consulting company “Loze&Kokins” prepared the research of WWF Latvia. The research is intended to promote a discussion and to exterminate the problem of illegal timber flow in Latvia.

Sources of Information referred to in the Foreword:

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1. Pre-logging stage

1.1. Forest inventory

Legal regulation

Forest inventory is considered to be an acquisition of information regarding the forest and documentation thereof. In accordance with the law, forest inventory is performed by persons who have the appropriate professional qualification.

The performance of inventory is one of the preconditions for the logging of timber to be started in the forest. Thus the owner of forest or legal possessor is obliged to perform a forest inventory at least once in 10 years in forests being in its property or possession and to submit the materials thereof to the State Forest Service. Information from the forest inventory is to be submitted to the respective Regional Forest District Office of the State Forest Service.

Arrangements of control

The data quality of forest inventory is examined by the State Forest Service. The State Forest Service works out and delivers to performers of forest inventory, forest surveyors, – input software of inventory data, structure of database, classifiers, algorithms for calculation of secondary parameters of forest stands and tables of codes.

A forest surveyor electronically submits to the State Forest Service appropriately prepared inventory data, as well as a description printout of forest inventory and plans of forestland inventoried.

The State Forest Service doesn't accept inventory data, if:

- the contents of the inventory do not correspond to the requirements prescribed in the Regulations of the Cabinet;
- during the examination in nature it is found that taxation elements and accuracy of sub-compartment identification exceed a possible deviation determined in regulatory enactments or they do not correspond to classifiers ;
- non-conformity between forestland plan and the sub-compartment description

"Gaps" in the legal regulation and possible violations

In our view, the frequency of information update on forest condition is incompletely regulated. For example, if the owner or a legal possessor of a forest has changed, the law does not require after the acquisition of a property or legal possession to provide information on the condition of the forest obtained in property or possession at the moment the owners change. Nor is such information obtainable from inventory data, because in such situation the law does not require a new owner/legal possessor to perform a routine forest inventory, if the term of validity of previous inventory has not yet expired (that is – the inventory has been performed more than 10 years ago).

Although it is determined that the State Forest Service prior to accepting inventory data must ascertain for itself the compatibility to the real situation, most frequently forest officials do not observe this legal requirement and affirm inventory data without the on-site examination. Besides, by experience of practice, until now there has been no case where a license of any of the companies providing inventory services had been annulled because of non-observance of quality requirements of the services provided.

Normative regulations in force and Control mechanisms allow the following possible violations:

- a) forest surveyor in accordance with indications of a forest owner or legal possessor, compiles inventory data, indicating a smaller standing volume than exists in nature. Following such inventory data a felling license based on such data is issued. As a result a larger volume of timber can be felled;
- b) forest surveyor in accordance with indications of a forest owner or legal possessor, compiles inventory

data, indicating larger standing volume than exists in nature. Based on such inventory data, the necessary documents for legal logging are issued and they can further serve as a basis for activities with illegally acquired timber.

Responsibility for non-observance of legal regulations

Normative regulations determine that the forest owner or legal possessor is responsible for veracity of inventory data, but no regulatory enactment determines the procedures by which those forest owners/legal possessors who do not observe the requirement of the referred to law and provide false information on forest inventory or do not provide such information at all can be called to answer for their deeds.

In accordance with the Criminal Law (CL), a forest officer who has not fulfilled his service duties and has not examined on-site if the inventory data corresponds to the real situation, can as a state office holder be brought to justice in accordance with those articles of the CL that foresee liability for criminal offences committed whilst in the service of a state institution, if through his or her action, substantial damage has been caused to state power or the order of a local government or to the rights and interests of a person protected by law, as well as for the forgery of documents. Likewise, a forest official can be held disciplinarily liable for the inadequate fulfilment of his service duties.

The procedures provided for in regulatory enactments by which a performer of forest inventory can be brought to responsibility if it is discovered that the referred to person has deliberately (in accordance with the interests of a forest owner or legal possessor) promoted the erroneous compilation and registration of data is incomplete. Thus, a performer of forest inventory can be only be called to responsibility in accordance with those regulatory enactments that provide for liability for violation of consumer's rights, namely, for providing poor quality services.

Recommendations

Referring to legal regulations:

- to introduce a provision in case of a change of a forest owner/legal possessor to submit to the State Forest Service an extraordinary report that has been approved by a signature of a forest officer, on the on-site situation of the forest at the moment of a change of a forest owner/legal possessor;
- to introduce a supervision institution for certified forest surveyors because the existing legal regulations do not provide for any concrete institution that would perform the control on forest surveyors concerning their conformity to professional criteria raised to them.

Referring to liability:

- to determine liability for forest owners and legal possessors who deliberately provide false information on forest inventory or do not provide such information at all;
- to determine the responsibility for licensed companies, which provide services related to forest taxation, concerning the quality of the services provided by their employees; it would be appropriate to work out a system of penalties determining that, for example, if it is fixed that an employee of the company, when performing his service duties, has not observed requirements of regulatory enactments, the Company can lose its operational license for a determined period of time.

Regulatory enactments taken into consideration for examination of the question:

- *Forest Law;*
- *Law on the State Forest Service;*
- *Criminal Law;*
- *Regulations of the Cabinet of Ministers No. 434 on the exchange of information concerning the State Forest Register;*
- *Regulations of the Cabinet of Ministers No. 109 on the professional qualification requirements for planning forest inventory and forest management.*

1.2. Furnishing of information on changes affecting forest land

Legal regulation

A forest owner or legal possessor has a duty every year by the 1st February to inform the State Forest Service regarding such changes as have affected forestland during the previous year:

- on activities for performance of which a license was necessary;
- on forest damage;
- on forest regeneration;
- on forest establishment;
- on thinning of young stands.

The referred to report is submitted to the relevant Regional Forest District Office of the State Forest Service, in the territory of which a forest property or legal possession is situated. When submitting the report a forest owner or a legal possessor (authorized person) certifies with a signature that he has informed the State Forest Service regarding all activities, performed in the concrete property of the territory surveyed by the forest authorities, regarding which he should inform the referred to agency. If an owner of forest submits several reports during the year, the respective reference is referred to in the last report.

The report is submitted also in such cases when approval is received, but the respective activity has not been performed.

Arrangements of control

The State Forest Service examines and supervises the veracity of submitted information. After the review of submitted documents and the examination on-site, the State Forest Service records the submitted information in the State Forest Register or issues a motivated written refusal to an applicant within one month

The failure to submit information on a timely basis is one of the preconditions for the State Forest Service to have the right to refuse to issue a license to a forest owner or legal possessor.

“Gaps” in legal regulations and possible violations

The existing normative regulations and arrangements of control allow the following possible violation, namely, the owner or legal possessor has changed for the relevant forest. The previous owner or legal possessor has not performed his duty, by providing the information required by law, thus a new owner or legal possessor indicates in the report submitted to the State Forest Service that, for example, damage has occurred to the forest during the previous year, as a result of which the standing volume has diminished, the fact regarding which information was not provided by the previous owner or legal possessor. As a result, the new owner or legal possessor can illegally fell as many trees as “have disappeared” from the forest during the period when the forest had not yet come into his ownership or legal possession.

Responsibility for non-observance of legal regulation

There is no liability provided for a forest owner or legal possessor in the regulatory enactments, if the information referred to previously has not been submitted in good time or has not been submitted at all. Currently the only reason that forces forest owners and legal possessors to comply with the requirement of the law regarding the submission of information is that if such information is not submitted, the State Forest Service has the right to decline the license requested.

Recommendations

Concerning liability:

- to provide for the liability of forest owners and legal possessors in the Code of Administrative process (CAP) in case they do not submit, timely or at all, to the State Forest Service the information provided by the law.

Regulatory enactments according to which the examination has taken place:

- Forest Law;
- Regulations of the Cabinet of Ministers No. 434 regarding the exchange of information related to the State Forest Register;

2. Logging

Legal regulation

A license is a document issued by the State Forest Service certifying the legality of specific planned activities and is to be considered as the permit for this activity.

In order to start the logging of timber in the forestland, a license is necessary, except in cases when the trees with the stump diameter of less than 12 cm as well as dead and wind-fallen trees are felled for thinning purposes. The volume of dead and wind-fallen trees felled without a license in the relevant territory of the forest district that is in an existing property or is in legal possession may not exceed 10 cubic meters in a year.

If the felling of trees is required in emergency situations (snowstorm, windstorm that is disturbing the action of infrastructure, limitation of fires and other cases determined by the law) the felling can be started after an oral announcement to the State Forest Service. The license is issued after the felling site has been examined in nature.

In order to receive a felling license, the forest owner or legal possessor has to submit a felling application in the relevant Forest District Office of the State Forest Service in the territory of which the forest property or legal possession is located. The application has to contain the following information:

- Applicant – the given name, surname and identity number of a natural person or the name and registration number of a legal person;
- If the applicant is not the owner or a legal possessor of a forest – the given name, surname and personal code of an authorised person, the number of the warrant, date of issue and the institution that issued the warrant;
- In all cases the name of a farm (structural unit), symbol of cadastre of a land unit, parish and the year of the last forest inventory;
- The felling method (for the main felling it should be supplementary referred to the form of execution of a cutting – clear cutting or selection cutting)
- The number of the felling site (numerate in the application), forest compartment and sub-compartment number;
- Area (ha);
- Dominant species (by the inventory data)

If there is an application for a clear cut, the pine seed trees to be left, the volume (m³) of the timber to be felled should be indicated for the main felling and a sketch of a felling site should be additionally submitted (scale 1:10000) for the reconstructive felling. For other cuts in cases of the transformation of forestland into other land uses, the permit of forestland transformation is attached.

The license is issued within one month after receipt of the application of a forest owner or legal possessor and it is valid until the 31st December of a current year. The payment for a receipt of a license is Ls 1.

Control mechanisms

The State Forest Service performs the control of the order of issue of a felling license. The employee of the State Forest Service issues a felling license to a forest owner or a legal possessor, or to his authorised person only after he has examined the conformity of a declared action to the regulatory enactments and a situation on-site. If a declared action doesn't conform to requirements imposed by the legal acts, a forest officer or his deputy issues to an applicant motivated written refusal to issue a felling license.

So, the license is not issued if:

- the planned action does not conform to the requirements of legal acts;
- a forest owner or a legal possessor has not indicated the definite information in the application or has not submitted the information on activities whose performance needs a license, as well as has not submitted

the information on – forest damage, forest regeneration , forest establishment, thinning of young stands;

- forest owner or a legal possessor has not submitted materials of forest inventory.

A forest owner or a legal possessor (or an authorised person) is informed that the information on the performed management activities should be submitted by the 1st February next year. After the receipt of information (on management activities), the felling license is filed in a case of the relevant forest owner or legal possessor. The felling license is stored till the next forest inventory but not less than for 5 years.

“Gaps” in legal regulation and possible violations

The normative regulation in force allows a situation in which a felling license can be obtained both by the forest owner (a person who has secured his ownership rights in the Land Registry) and the legal possessor (a person who has obtained the ownership rights to a specific forest on a legal basis (for instance, by way of a purchase agreement), but has not yet relevantly registered such in the Land Registry). Thus, a situation may occur when the forest owner sells his ownership rights to another person who doesn't hurry to register his ownership rights in the Land Registry, but performs an illegal forest logging in his newly obtained forest the next day. Legally the responsibility for this goes to the previous forest owner, because he is merely the owner of a definite forest property in accordance with Latvian Civil Law. In order to avoid a conflict between special and general legal norms, see the recommendations concerning legal regulation.

The existing normative regulation and Control mechanisms allow the following violations (unwarranted felling):

- a) trees are felled without the issued felling license;
- b) felling is performed exceeding the amount indicated in the felling license.

Detailed commentary would be necessary for the situation described in point b). Such violation is possible in the following cases:

- 1) as the current normative regulation determines that forest inventory must be performed at least once in 10 years, based on the outdated inventory data where, for example, the standing volume to be felled is determined smaller than it is on-site at the given moment, the felling license is issued to this volume. But in reality during these 10 years the stock to be felled has increased in this forest. As a result the volume illegally felled is equal to: the standing volume on-site minus the volume indicated in the felling license;
- 2) normative regulation provides that a forest owner or a legal possessor must submit the information on the changes affecting the forest annually by the 1st February. But in the case when the forest owner or a legal possessor has changed, it transpires that the previous owner or legal possessor has not submitted such information to the State Forest Service. Thus a new owner or legal possessor has a possibility to submit false information, namely, even though the volume to be felled is larger on-site, he can declare that last year when the forest was not yet under his authority, the forest was damaged or illegal felling has occurred, as a result of which certain m³ have been 'lost' from the stock. Finally so many m³ of the stock are felled, that are equal to: the volume on-site minus "lost" m³.

During the discussions with specialists from the sector, the opinion was expressed that the problem exists with the aspects of legal liability in those cases in which only the felling rights are sold without the ownership rights on the forestland. When examining this question from the legal point of view, as well as finding out the court practice, we discovered that in reference to the mentioned situation, the 'gaps' in the legal regulation have been liquidated for the time being (see the next section).

Liability for non-observance of legal regulations

There is an administrative liability provided for in the second paragraph of Article 67 of the Code of Administrative Offences (COA) – unwarranted felling of growing trees. This form of liability is to be applied to forest owners or legal possessors, but only in the case if the offence qualifying conditions of felling provided in the second and third paragraphs of Article 109 of the Criminal Law are not established. The penalty provided in COA is a fine - up to Ls 250.

The liability is provided for unwarranted felling in the alien forest under the first paragraph of Article 109 of the CL. The alien forest has to be understood as the forest that has been secured in the ownership of other

person or has been delivered into other person's legal possession. So, in accordance with the first paragraph of Article 109 of the CL the alien persons are called to justice, but not the forest owner or legal possessor. The penalty, provided in the first paragraph of Article 109 of the CL, is a deprivation of freedom to the period up to 4 years or the arrest or forced labour, or a fine up to 80 minimal monthly wages.

There is a liability provided in the second paragraph of Article 109 of the CL for unwarranted felling in the state specially protected nature territory or object, park, dendrologic object, land or water protective zone, in city green area. In contrast to the first paragraph of the article to be commented upon, the illegal activities referred to in the second paragraph of the article, are criminally punishable depending on the fact whether it is the forest owner, legal possessor or alien person who has performed them. The prescribed punishment is a deprivation of freedom up to 6 years or a fine up to 100 minimal monthly wages.

There is a particularly qualified crime content provided in the third paragraph of Article 109 of the CL – unwarranted felling if such action has created significant damage. The significant damage can be estimated by the value of the felled trees, quantity of trees and significance of the species, destruction of forestland, non-collecting of tops and lops and other logging residues, as well as proliferation of tree pests related to the lack of cleanup of the felling site etc. Also in this case any person, who has committed these activities, is held responsible. The punishment for the commitment of these activities is a deprivation of freedom up to a period of 10 years or arrest, or a fine up to 150 minimal monthly wages.

In accordance with the Forest Law and Latvian Civil Law, if a forest owner/legal possessor has granted a right to forest harvesting (without land ownership rights) to another person, this fact doesn't release the forest owner/legal possessor from the material responsibility for the forest offence done by his contractor. As the felling license is issued to the forest owner/legal possessor, he has to monitor the action of the logging operator, so that he would observe the conditions of the felling license. If as a result of illegal felling, a criminal offence has been detected during the committing of which the logging operator has to be blamed then the forest harvesting manager will be held criminally liable as a subject of this offence, but the civil liability will be applied to the forest owner/legal possessor for the tolerated forest offence in the forest of his ownership or legal possession. The forest owner/legal possessor will have to remunerate the damage caused in favour of the state (second paragraph of Article 50 of the Forest Law) in accordance with the order provided in the Regulations of the Cabinet of Ministers No.370 Order by which the damaged caused to the forest has to be remunerated.

Recommendations

In reference to the legal regulation:

- in order to eliminate the situation, in which the legal possessor immediately after the acquisition of forest into ownership, fails record accordingly the ownership rights into the Land Registry, could start the felling, it would be advisable to legally enforce the following requirement – the felling license can be delivered solely to a forest owner who has accordingly registered his ownership rights in the Land Registry. Before the implementation of such a requirement it would be necessary to examine the socio-economic factors determining whether it possible to provide this requirement practicable also from a financial perspective.

In reference to the control arrangements:

- it would be necessary to exact more stringent control over the compatibility of the information to the regulatory enactments and the real situation on-site that has been indicated by the forest owner or a legal possessor in the felling license. Particular attention should be also paid to the compatibility of data with the real situation on-site, provided by the forest owner/legal possessor straight after the end of the management (felling) activity – whether the rules indicated in the felling license are observed.

In reference to the liability:

- in the existing normative regulations it would be useful to ensure that the information should be summed up in the State Forest Register regarding all law breakers who have not observed in their activities the conditions prescribed in the regulatory enactments regulating felling activities. It should be necessary to

strengthen a principle in the law whereby such lawbreakers would be deprived temporarily from the rights to obtain the felling license.

The legal acts serving for the examination of this question:

- *Forest Law;*
- *Latvian Civil Law/section of obligations and affairs;*
- *Criminal Law;*
- *The Code of Administrative Offences of Latvia;*
- *Regulations of the Cabinet of Ministers No. 434 on the exchange of information concerning State Forest Register;*
- *The State Forest Service Ordinance No. 338 on validation of specimen of forms of licenses, applications and reviews;*
- *The plenary decision No. 6 of the Supreme Court on the application of law in criminal cases on illegal (unwarranted) felling, forest destruction or damaging.*

3. Timber trade and the related services

3.1. Delivery to the recipient

Legal regulation

Concerning the timber delivery, the Parliament and the Cabinet of Ministers have prescribed a comparatively severe normative order, the basic elements being the following:

(a) bill of lading for timber transportation

Any delivery of timber can legally take place only if the supplier has executed a special bill of lading for timber transportation (BLTT). In contrast to the general bill of lading, when drawing up a BLTT the following supplementary data has to be provided:

- Felling license*;
- Place of cargo loading and unloading;
- Cargo carrier.

**Only the first supplier must provide data on the felling license. Namely, a timber purchaser (a middleman) can form the further supply without determining the initial origin.*

It is necessary to note that BLTT has to be made not only for timber supply, but also for any services that are related to timber preparation, treatment, processing, transfer and storage.

BLTT must be drawn up both by natural and legal persons apart from the fact whether the definite person has been registered as a tax (value added tax (VAT)) payer. This requirement means that neither a timber supply nor a transfer nor other services may be performed without a BLTT. However, the State Forest Service is exempted from the executing the BLTT, when issuing felling licenses.

The numerated BLTT forms are issued by the State Revenue Service (SRS), where they are appropriately registered.

(b) BLTT registration journal

The data on all issued and received BLTT are to be registered into a special BLTT registration journal, that is to be kept in the places of timber storage or in the places where services are provided (in sawmills, warehouses etc).

(c) Reporting on the BLTT use

A person, who has received a BLTT at the SRS, must submit a report on the use of all received BLTT to the territorial office of the SRS.

(d) special VAT regime

The Parliament has determined a special order of application of VAT for timber supply and for services related to this supply, the essence of it is the following: a supplier of timber or a provider of relevant services completes a BLTT, but doesn't pay the sum provided in it in the budget of VAT and reduces the sum that is required from the timber (services) recipient. But the recipient of timber pays the sum indicated in the BLTT in the budget, at the same time reducing his pre-tax. The regulatory enactments also provide a special order for completion of VAT declarations and their annexes in the area of timber supply and the services related to it. The special VAT regime has an aim to maximally limit the fictitious supply and the fictitious reflection of pre-tax sums in the VAT declarations and accordingly the unfounded reduction of the tax payable in the budget.

Control mechanisms

The application of VAT and its payment, the general use of BLTT, as well as the maintenance of registration journals, is controlled by the SRS. In the opinion of the SRS, the results of the examinations may be submitted to the Finance Police for the performance of an inquiry.

The "gaps" in the legal regulation and examination of possible violation

As already referred to, any timber supply and the services related to it, starting from the assignment of felling rights and finishing with transportation to the producer or the customs office, must be formatted by BLTT. That means – the legal regulation of timber supply basically is directed to the maximal limitation of illegal timber flow. At the same time it means also that an illegal timber flow can be theoretically carried out in one of the following forms:

- a) BLTT is not drawn up on timber that is initially obtained without a felling license;
- b) BLTT is not drawn up on timber that is initially obtained exceeding the amount indicated in a felling license;
- c) On all above referred to supply, a falsified BLTT is made;
- d) Less timber is declared than is supplied in reality;
- e) A recipient of timber fictitiously rejects a part of the received cargo, however the fictitious part is not taken out of the further circulation.

The violations referred to in paragraphs a) – d) represent a logical continuation of the offences performed in the pre-logging and logging stages, and they can be evaded (limited), by putting into order a legal regulation and Control mechanisms in the pre-logging and logging stages, and of course, applying more effective control measures in the stage of timber trade under consideration (the examination of these stages will follow).

But in paragraph (e) the offence is possible because of deficient normative base concerning the return of the rejected timber. The SRS notes that the fact of a rejection can be confirmed by a statement, signed by the supplier and the recipient. The further return of the rejected product is possible using the initial bill of lading. The current order allows a situation, where:

- a timber supplier "destroys" the rejected cargo, although he has sold it to the recipient;
- a timber recipient retains the rejected cargo in the illegal turnover.

The liability for the non-observance of the legal regulation

In accordance with the Law on Duties and Taxes, if the tax base is reduced, the SRS counts and collects from the trespasser the reduced tax sum and a fine in the amount thereof is made over in the favour of the budget.

The liability is determined in the CAO for:

- non-observance of the turnover order of the goods (services), accounting and bills of lading – the fine depending on offence qualifying conditions is from Ls 100 – Ls 250, as well as the confiscation of goods can be applied (Art.155.1.);
- non-observance of conditions of the order of book-keeping – a fine from Ls 100 – Ls 150; for evading to submit the referred to bookkeeping information or documents – a fine from Ls 150 – Ls 200 (Art.166.6.).

In accordance with the CL:

- According to Article 217 the persons are called to justice if with their action or inaction they have repeatedly during one year breached the conditions of the order of book-keeping, penalty – forced labour or a fine up to 20 minimal monthly wages; if persons have carried out the hiding or fraudulence of the documents of book-keeping – they can be punished with a deprivation of freedom up to the period of 3 years or with a fine up to 80 minimal monthly wages;
- According to Article 218 the liability is provided for evading of payment of taxes or charges made equal to taxes, for hiding or reducing of income, profit or other taxable object, if these activities have been carried out repeatedly in a year's time, penalty - deprivation of freedom up to 3 years or arrest, or a fine up to 80 minimal monthly wages, denial of the right to engage in entrepreneurial activity for a period from 2 up to 5 years or without it. If the losses have been caused to the state or a municipality in great amount – carries a deprivation of freedom up to 5 years or with a fine up to 120 minimal monthly wages, confiscating a fortune or without it, depriving rights to carry out entrepreneurship activity from the period of 2 years up to 5 years or without it;
- If false information is provided in the BLTT – the relevant persons are called to justice in accordance with Article 275 of the CL for the fraudulence of documents and the use of false documents – punishment – deprivation of freedom up to a period of 2 years or arrest, or forced labour, or a fine up to 40 minimal monthly wages. If the offences have been carried out repeatedly or with an intent of acquisitiveness, or if they have been carried out by a group of persons by a prior agreement, or if they have caused significant damage to the state or governmental or to the interests and rights of persons protected by the law, - carries a deprivation of freedom up to 4 years or with a fine up to 60 minimal monthly wages.
- The relevant persons responsible for fraudulence of documents are called to justice in accordance with Article 275 of CL (see the previous paragraph). Civil rights organisations have not reached agreement regarding whether Article 275 should be applied to the producer of a false BLTT.

Recommendations

In reference to legal regulations:

- determine the order for turnover for the rejected timber.

In reference to control arrangements:

- in our view, the SRS insufficiently carries out the functions provided in the law and uses the opportunities offered by the law, in order to analyse the flow of illegal timber, to carry out examination on the basis of analytical material and accordingly punish the trespassers. The SRS checkups in forest harvesting and wood processing should be organised according to the timber flow. Namely, in co-operation with the State Forest Service all stages of the timber flow should be subjected to the examination, starting with a control how the felling licence is realized and the use of the logged amount and tracing the further activities with a definite amount of timber up to it is supplied to the end user or taken to the customs control. All legal and natural persons, engaged in the relevant timber flow, should be subjected to such examinations;
- A single bill of lading-invoice was introduced in 1996 (bills of lading of timber – in 1998), but since their introduction the falsifiers of bills of lading have never been really punished. The law enforcement authorities should draft a practicable action plan for the detection of illegal typographic action and for calling to justice the culpable persons.

In reference to liability:

- to specify the wording of Article 275 of the CL, in order to eliminate doubt on the question, if the production of false BLTT has to be qualified as fraudulence of documents.

The legal acts serving for the examination of this question:

- *Law on Taxes and Duties;*
- *Law on Value Added Tax;*
- *Criminal Law;*
- *The Code of Administrative Offences of Latvia;*

- *Regulations of the Cabinet of Ministers No. 251 "The order by which the value added tax is applied to the activities with a timber";*
- *Regulations of the Cabinet of Ministers No. 252 "The order of the use and processing of the bill of lading-invoice".*

3.2. Accounting and physical registration of timber

Legal regulation

There is not a special, different method determined for the registration of timber stock in the finance bookkeeping. The legal person may choose one of the methods of registration of allowances of the stocks determined in the law: method of weighted average price or FIFO method. However this requirement does not refer to farms and individual enterprises, the annual income of which do not exceed Ls 45,000, as well as to self-employed persons. The persons of referred to categories have the right to choose any registration method they want.

There is not a legally binding method for the physical registration of timber stocks. Undoubtedly, both during the pre-logging stage, when estimating the volume of standing timber, and in wood processing when measuring the amount of the processed material, there exist wide possibilities to manipulate with a correct application of a unit of measure "m3". In practice very frequently the amount of timber or timber to be measured is determined on sight. A similar rules-absent situation can be observed also referring to the admissible norm of waste material in sawmills, where frequently the volume of ready-made product in solid cubic meters differs substantially from the volume of round timber consumed as raw material.

Control arrangements

The conformity of the registration of timber stock to the legal requirements insomuch as it refers to tax matters, is controlled by the SRS. In our view, the conformity of physical registration of timber is not controlled at all.

The liability for non-observance/trespassing of legal regulations

See Section 3.1.

Recommendations

In reference to the legal regulations:

- It is possible that in timber harvesting and wood processing more severe requirements in relation to the recording of stocks should be introduced, as well as the order and periodicity of inventories;
- It is possible that the rules of accounting should be applied also to the category of persons who are currently exempt from this regulation (farms and individual enterprises with the annual income not exceeding Ls 45,000, as well as self-employed persons);
- The binding method for the determination of a unit of measure (m3) for timber and timber products should be prescribed.

In reference to the liability:

- more effective punishments should be prescribed for the distortion or fraudulence of accounting data and documents, if a direct or indirect result of such action is a significant damage to the state (municipal) budget or natural resources.

The legal acts serving for the examination of this question:

- *Law on Accounting;*
- *Law on Annual Reports of Enterprises;*
- *Criminal Law;*
- *The Code of Administrative Offences of Latvia.*

3.3. Settlements

Legal regulations

Settlements between a timber recipient and a supplier, as well as a provider of service, may be carried out solely by the mediation of banks. The cash deposits in the cash department of a supplier are prohibited.

Control mechanisms

The order of settlements inasmuch as it refers to tax matters, is controlled by the SRS.

The “gaps” in the legal regulations and examination of possible violations

The regulatory enactments forbid the cash settlements in the areas of wood processing and timber harvesting (except non-significant transactions* and settlements among natural persons, who are not VAT payers). Thus, one can say that the “gaps”, allowing the legal or semi-legal evasion of the statutory order, do not exist in the legal regulations. Accordingly any cash settlements are to be qualified as a deliberate violation of a legal order.

**Non-significant transactions – the payments of natural persons not exceeding the value of Ls 20.*

It is possible that the most significant source of the non-registered cash is those natural persons who provide various services to the buyers of timber. The scheme of raising non-registered cash could be as follows:

- the company A writes out a bill to a company B (a timber purchaser) for fictitious services ;
- B transfers the sum required in a bill to the account of B;
- A delivers to B cash in the sum, that is less than the one received by non-cash. The difference can be conventionally named as a payment for the purchase of non-registered cash.
- B uses “the purchased” cash for the settlements of illegally obtained timber.

The following can be referred to as the possible sources from which the service providers obtain the non-registered cash:

- (a) The providers of services or other companies related to them obtain non-registered cash income in such traditionally difficult-to-control areas as retail trade, public catering, building, games of chance and in other areas of final consumption, where a client or a buyer is a resident (**Fig. 1**);
- (b) The providers of services are fictitious companies (**Fig. 1**). The fictitious companies are usually established with intent to defraud the value-added tax from the state. The fraudulent schemes linked to VAT can be more or less complicated, but the basic scenario is normally like this:

The normal founder of a fictitious company is a natural person, who is either unidentifiable (false passport) or he is a person without a definite place of residence and occupation. The fictitiously founded company provides fictitious services to other companies. The VAT obtained from such services (as well as a company income tax) is not paid in the state budget. The sum collected from the recipients of “services”, also VAT, is withdrawn in cash whereupon the fictitious company terminates its activity (dissolves itself). It should be noted that the recipients of “services” have the right, even on these conditions, to refer to a deductible pre-tax the VAT sum that has been paid to the fictitious company.

- c) the providers of services or other companies related to it obtain non-registered cash income from the “offshore” structures belonging to them (**Fig. 2**).

Fig. 1

The sources of illegal cash – domestic companies of the consumption branches or fictitious companies



The company of the end-use sector or a fictitious company

A bill for fictitious services for 100 Ls

Settlement of the bill via bank – 100 Ls

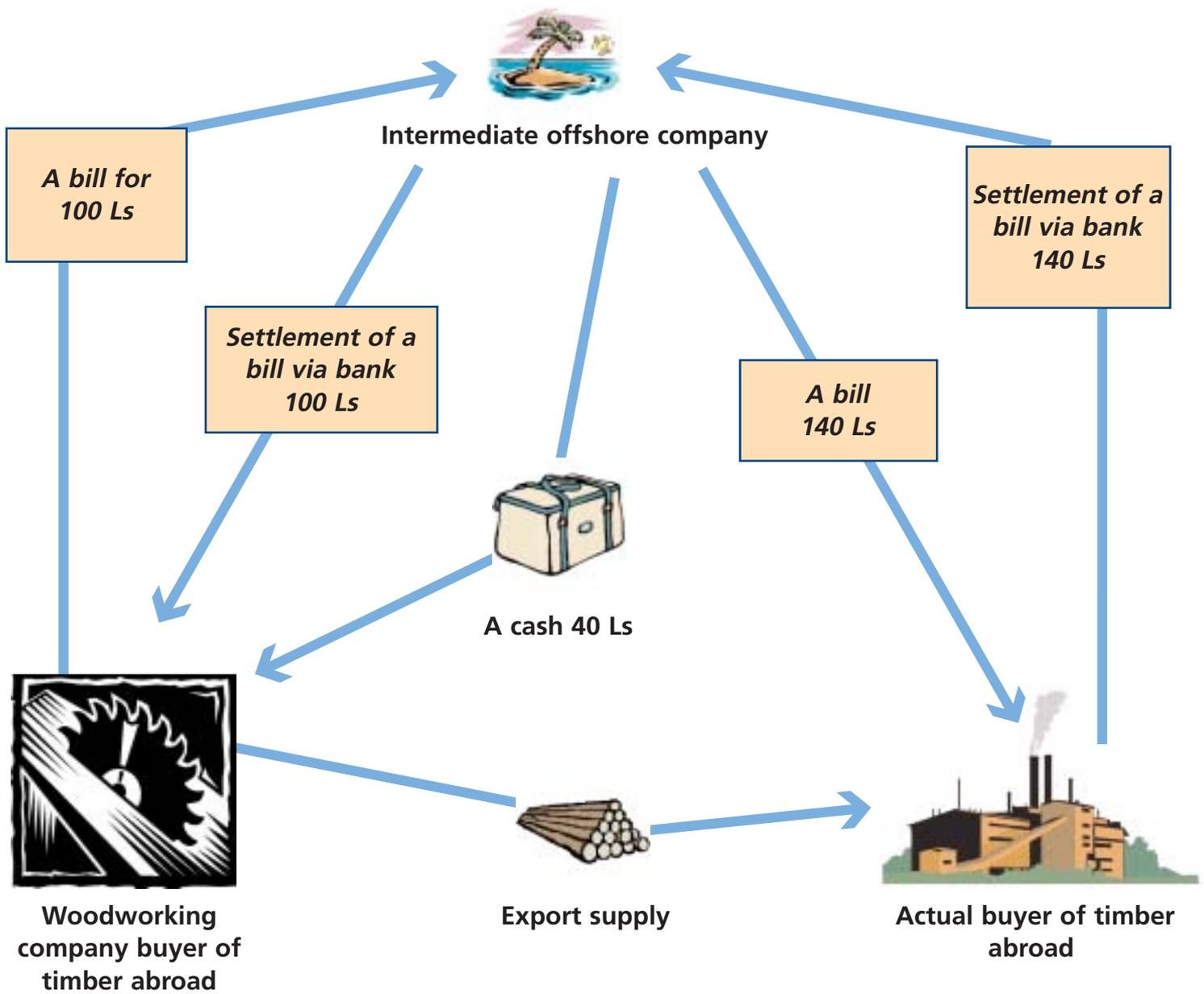
The illegal cash 90 Ls



The woodworking company

Fig. 2

The sources of illegal cash – “offshore” companies



The liability for non-observance/violation of legal regulation

There is a liability provided in the CAO for non-observance of the order of clearing – for such a violation a fine can be applied from Ls 150 – Ls 250 (article 156.3.).

It is somewhat surprising that there is no criminal liability regarding the illegal use of cash in settlements.

Recommendations

In reference to control measures:

- Taking into account that in the initial source (in the branches of end use) the illegally obtained cash serves as a form of settlement for a chain of other illegal activities (the wood processing and timber harvesting sectors are probably not the biggest consumers of illegal money), the government should work out a plan to combat illegal turnover of cash on the national level;
- For the examinations that are to be carried out in the branches of wood processing and timber harvesting, the SRS could work out a special method in accordance with which the range of services provided in the sector, providers of services and the relationship of a provider of services or its owner to the branches end-users as potential sources of gain of illegal cash would be subjected to the detailed examinations and valuation of the content thereof.

In reference to the liability:

- to provide the criminal liability for transactions in cash, the aim of which is to disburse or to finance illegal action.

The legal acts serving for the examination of this question:

- *Law on Duties and Taxes;*
- *Criminal Law;*
- *The Code of Administrative Offences of Latvia;*
- *Regulations of the Cabinet of Ministers No. 251 "The order by which the value added tax is applied to the activities with a timber";*
- *Regulations of the Cabinet of Ministers No. 252 "The order of the use and processing of the bill of lading-invoice".*

Summary

Illegal timber logging and trade can be carried out because of various negative pre-conditions. However, the most important of all is the offer of illegal cash in the "grey" and "black" economy. If the illegal cash would not exist, the motivation for illegal logging would disappear.

The offer of illegal cash creates or provokes the chain of all other illegal activities: counterfeiting bill of lading, falsification of bookkeeping facts, tax evasion, furnishing of false forest inventory and information, manipulations with forest ownership rights (tenure rights) and eventually – illegal timber logging.

In our view, the sources of origin of illegal timber are to be found both in the stage of forest utilization and timber processing. Concerning the timber processing stage there are at least two possible scenarios of illegitimacy (**Fig.3, 4, 5**):

Fig. 3

Scenario A: the sources of illegal timber in the stage of forest exploitation

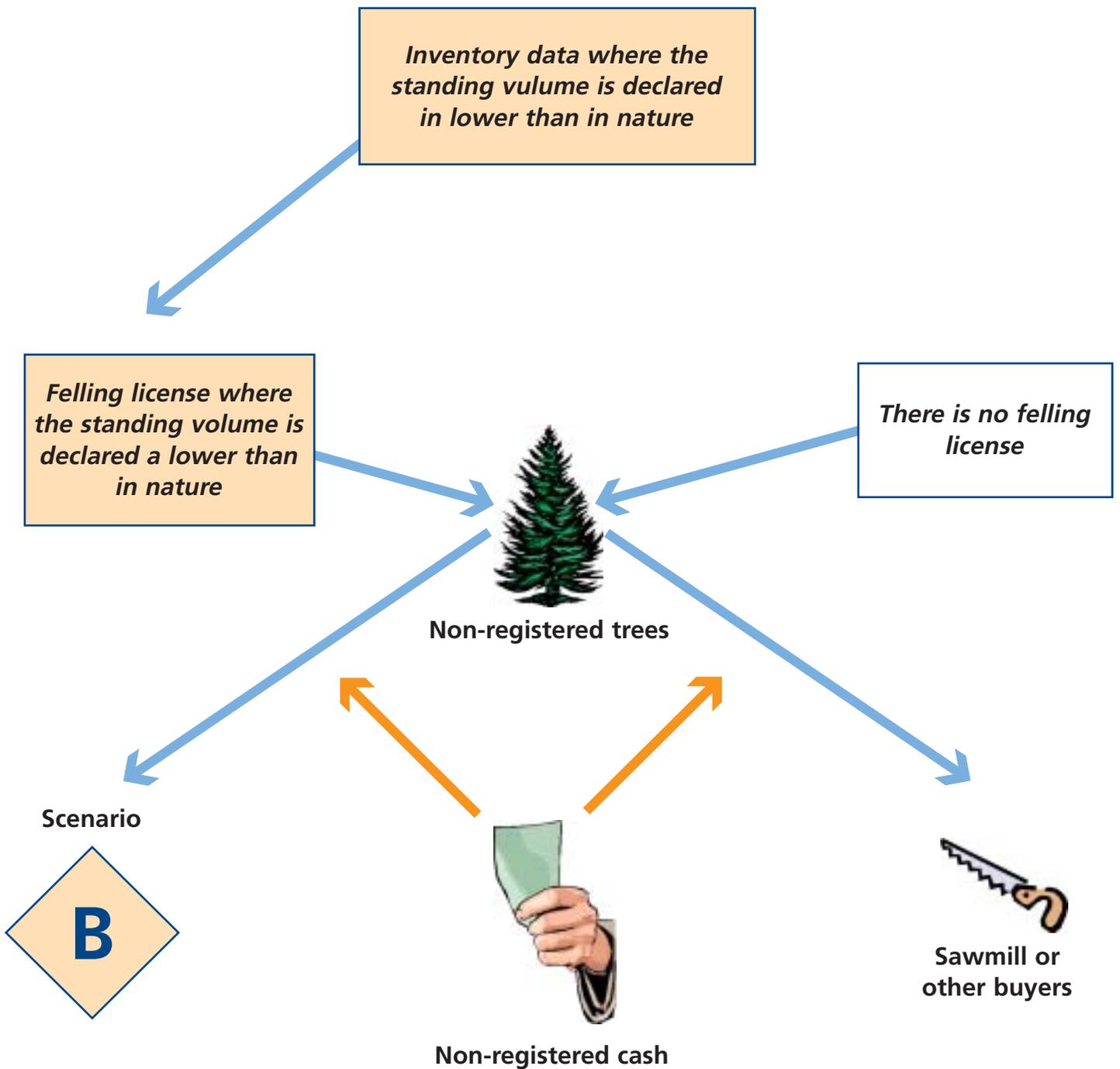
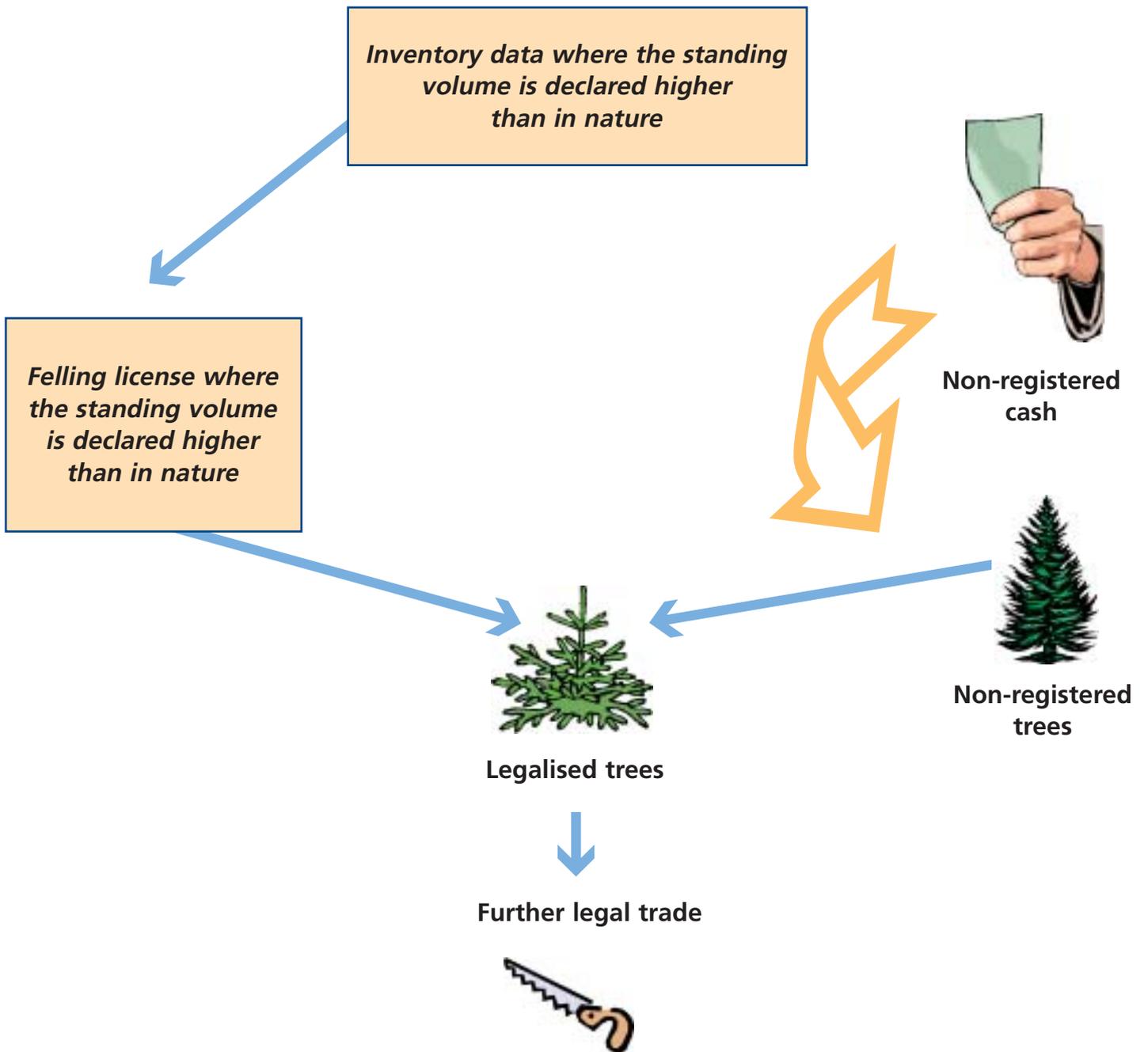


Fig. 4

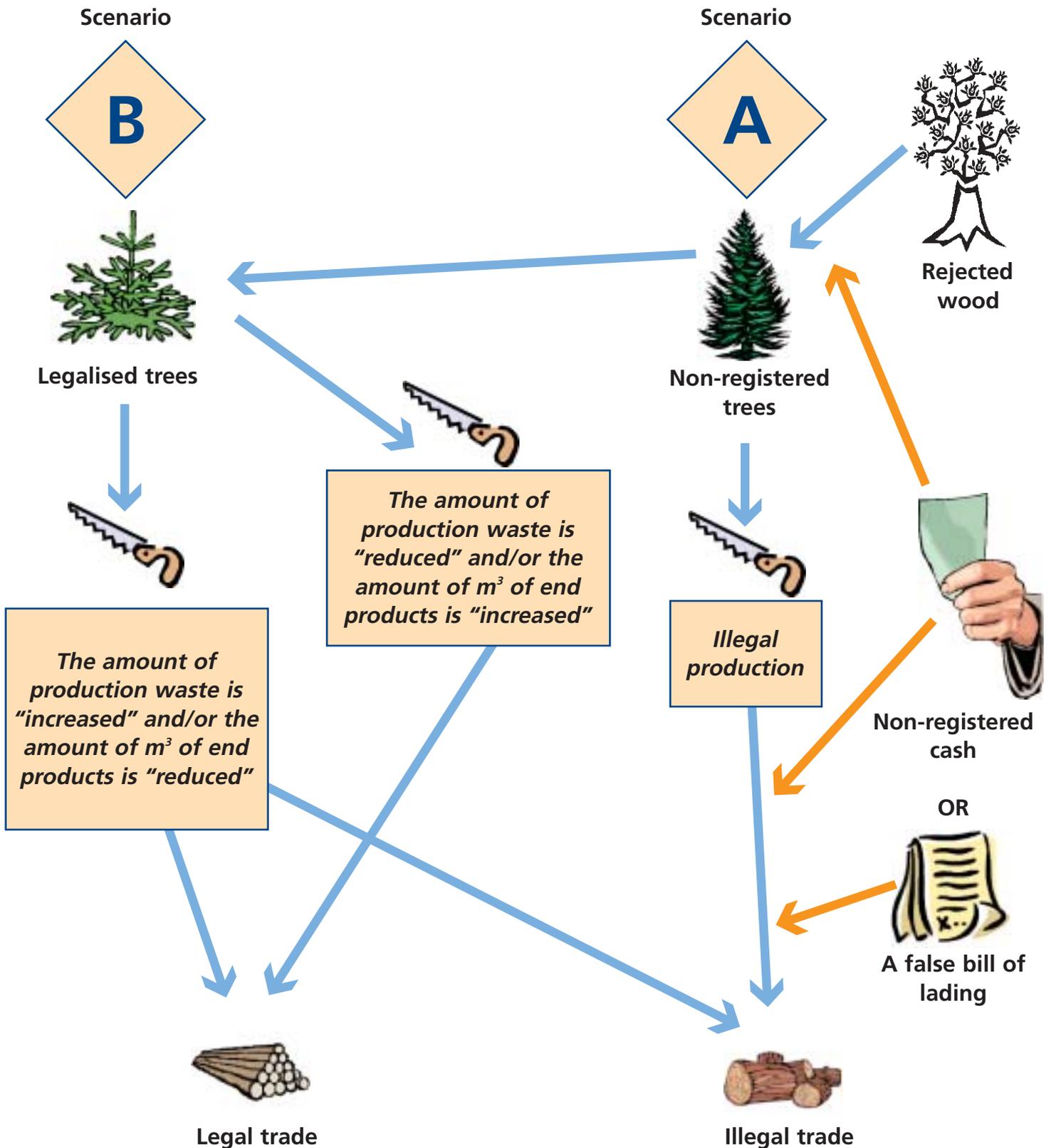
Scenario B: the legalization of the illegal timber in the stage of timber harvesting



The sources of illegal timber flow in the stage of timber processing are reflected in the following scheme:

Fig. 5

The sources of illegal timber turnover in timber processing



As long as the offer of illegal cash exists, it will not be possible to completely eradicate the illegalities in wood processing and timber harvesting. However, it is possible to restrict illegalities provided that at the government level:

(a) The sectors of wood processing and timber harvesting are considered to be the crisis sectors which:

- generate non-registered cash;
- are significant consumers of non-registered cash;
- are insufficiently controlled by the state institutions;
- the liability of the violence of legal norms is not provided in many cases;

the result of which is a plunder of not only state financial resources, but different from other sectors – the nature is being damaged as well;

(b) a complex plan is worked out in order to restrict the generation and turnover of illegal cash;

(c) a complex plan is worked out in order to restrict the illegalities in the wood processing and timber harvesting sectors that would at least contain the following arrangements:

- the accomplishment of analytic work of the SRS;
- the elaboration of a special method of tax audit corresponding to the “routes” of illegal timber flows;
- to accomplish the legal regulation relating to the forest inventory, to the issue of felling licenses; storage, processing and accounting of timber;
- to perform an inventory of the current legal liability norms, providing punishment for those illegal activities, that do not have penalty sanctions in legislation at all, and to strengthen the liability in reference to those illegal activities, for which the current penalty sanctions are estimated as too lenient.

The further research of pre-conditions of illegal logging of timber and the preparation of suggestions for stamping out the breach of law should be performed in the following directions:

- the research into procedures of import, export, transit and temporary importation and finding out of the possible malicious activity related to transactions with timber;
- the preparation of proposals in the area of book-keeping, especially concerning the valuation of timber stocks;
- the preparation of detailed recommendations for examination to be carried out by the SRS in the wood processing and forest harvesting sectors;
- drafting the specific amendments of the regulatory enactments.

The summary of recommendations

Stages	Recommendations	Responsible institutions			
		Parliament	State Forest Service	State Revenue Service	Finance policy and other right protection institutions
1. Pre-logging stage	1. To implement the requirement that in case of change of forest owner/legal possessor an non-scheduled report (signed by a forest official) should be submitted to the State Forest Service on the situation of forest in nature as to the moment of the change of forest owner/legal possessor;	Implementation of normative base	Surveillance on information turnover		
	2. To establish a supervisory institution for certified forest surveyors performing forest inventory, because the current rules do not determine any institution that would a control professional criteria required to forest surveyors	Implementation of normative base			
	3. Determine the responsibility of forest owners/legal possessors who knowingly provide false information on forest inventory or do not provide such information at all	Implementation of normative base	Call to justice		
	4. To determine the liability for licensed companies, providing services related to forest inventory, taxation, and forest estate valuation for the quality of work performed by their employees. The system of penalties should be worked out, determining that, for example, if it is fixed that an employee when performing his duties, has not observed the requirements of regulatory enactments, the Company can temporarily lose its licence	Implementation of normative base	Call to justice		
	5. To provide an administrative liability of forest owners/legal possessors in the Code of Administrative offences if they do not submit information in good time or at all, required by the law to the State Forest Service	Implementation of normative base	Call to justice		
2. Logging	1. In order to eliminate the situation, in which the legal possessor immediately after the acquisition of forest into the ownership, does not correspondingly register the ownership rights into the Land Registry, could start the felling, it	Implementation of normative base	To control the application of requirements of regulatory enactments		

The summary of recommendations

Stages	Recommendations	Responsible institutions			
		Parliament	State Forest Service	State Revenue Service	Finance policy and other right protection institutions
	would be recommendable to legally fortify the following requirement – the felling license can be delivered solely to the forest owner who has registered correspondingly his ownership rights in the Land Registry. Before the implementation of such a requirement it would be necessary to examine the socio-economic factors and whether it is possible to make this requirement practicable from a financial perspective.				
	2. It would be necessary to exact more stringent control over the compatibility of the information with the regulatory enactments and the real situation on-site that has been indicated by the forest owner or a legal possessor in the felling license. Particular attention should be also paid to the data compatibility with the actual situation on-site, provided by the forest owner/legal possessor straight after the end of the management (felling) activity – whether the rules indicated in the felling license are observed.		Control on the content of information		
	3. It would be worth to provide in the existing normative regulation that the information should be summed up in the State Forest Register regarding all law breakers, who have not observed the conditions provided in the regulatory enactments regulating timber logging in their activities. It should be necessary to strengthen a principle in the law whereby such lawbreakers would temporarily be deprived of their right to obtain a felling license.	Implementation of normative base	The summary of information		
3. Timber trade	1. Determine the order for turnover of rejected timber.	Concretisation of regulatory enactments			
	2. In our view, the SRS does not sufficiently carry out the functions provided in the law and does not sufficiently utilise the possibilities provided by the law, in order to analyse the illegal timber flow, to		Co-operation with the SRS – providing of information	Implementation of the Control mechanisms	

The summary of recommendations

Stages	Recommendations	Responsible institutions			
		Parliament	State Forest Service	State Revenue Service	Finance policy and other right protection institutions
	<p>carry out examinations on the basis of analytical material and to correspondingly punish those breaching legislation. The SRS examinations in the areas of timber harvesting and wood processing would be organised in accordance with the timber flow. Namely, in co-operation with the State Forest Service all stages of the chosen flow should be subjected to the examination, starting with a realization control of the felling license and the use of the logged amount and tracing the further activities with a definite amount of timber up to it is supplied to the end-user or taken to the customs control. All legal and natural persons, engaged in the relevant timber flow should be subjected to such examinations</p>				
	<p>3. A single bill of lading-invoice is introduced in 1996 (bills of lading of timber – in 1998), but since their introduction the falsifiers of bills of lading have never been really punished. Civil rights organisations should draft a practicable action plan for the detection of illegal typographic action and for calling to justice culpable persons</p>				Active deed in order to establish offences
	<p>4. To specify the wording of Article 275 of the CL, in order to eliminate doubt on the question of whether the production of false BLTT is to be classified as fraudulent preparation of documents</p>	Concretisation of regulatory enactments			
	<p>5. It is possible that stricter requirements should be introduced in timber harvesting and wood processing sectors in regard to stock-taking, as well as the order and frequency of inventories</p>	Perfection of normative base		Control on the observation of requirements	
	<p>6. It is possible that the rules of accounting should be applied also to the category of persons currently exempt from an obligation to report (farms and individual enterprises</p>	Perfection of normative base		Control on the observation of requirements	

The summary of recommendations

Stages	Recommendations	Responsible institutions			
		Parliament	State Forest Service	State Revenue Service	Finance policy and other right protection institutions
	with the annual income not exceeding Ls 45,000, as well as self-employed persons)				
	7. The binding method for the determination of a unit of measure (m ³) for timber and timber products should be prescribed			Drafting the method and control of its observance	
	8. More effective punishments should be prescribed for distortion or fraudulence of accounting data and documents, if a direct or indirect result of such action is a significant damage to the state (municipal) budget or natural resources	Perfection of normative base		Control	
	9. Taking into account that in the initial source (in the branches of end-use) the illegally obtained cash serves as a form of settlement for a chain of other illegal activities (the branches of wood processing and timber harvesting probably are not the biggest consumers of illegal money), the government should work out a plan combating the illegal turnover of cash at a national level	Drafting of action plan	Drafting of action plan	Drafting of action plan	Drafting of action plan
	10. For the examinations that are to be carried out in the branches of wood processing and timber harvesting, the SRS could work out a special method in accordance with the range of services provided in the branch, providers of services and the relation of a provider of services or their owner to the branches of the end-use as potential sources of gain of illegal cash, would be subjected to the detailed examinations and valuation of the content thereof			Drafting of method	
	11. To provide the criminal liability for transactions in cash, the aim of which is to disburse or to finance illegal action.	Perfection of normative base			