

# Forest and Grassland Task Force Report

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# Executive Summary

## INTRODUCTION

The Task Force appreciates the opportunity provided by the CCICED to provide an independent evaluation of the National Forest Protection Program and the Land Conversion Program, and to reflect more broadly on opportunities to strengthen the forestry sector. The Task Force applauds the Chinese government's recent efforts to transform the forest sector from a timber production orientation to one that is dedicated to restoring and conserving forest ecosystems and contributing to sustainable development. The Task Force believes that current programs and financial commitment of government are reflection of government's strong commitment to the ecological restoration of Western China while addressing the complex social income and employment implications for the forest-dependent households. These steps have the potential to establish a foundation for sustainable development in Western China and the Task Force wishes to make a positive contribution to this reform process.

This report summarizes the key findings of the Task Force during its second phase (2001-02). These findings were derived from an analysis of the implementation of the Natural Forest Protection Program (NFPP) and the Sloping Land Conversion Program (SLCP) conducted during the first phase; a set of policy studies commissioned in late 2001, and from the series of workshops and conferences conducted during this second phase. These findings are summarized and presented to the Council as a comprehensive framework for policy improvement and reform. This set of recommendations is intended to assist the Chinese government to improve the performance of the forest sector and achieve its goal of sustainable development while ensuring sustainable livelihoods for millions of forest-dependent people.

The recommendations<sup>1</sup> are organized into two parts below: (1) those directly pertaining to the NFPP and SLCP; and (2) those that pertain to the broader forest sector. The second set covers five policy areas recognized to be most critical to China's forest development: (1) forest governance and public administration; (2) taxation and fiscal policies; (3) forest tenure and ownership; (4) approaches to regulate forest harvesting and; (5) forestry and trade agreements. For each key policy area the framework presents: (1) existing policy issues; (2) policy reforms that can be implemented in the very short-term; and (3) research priorities.

This paper first reviews the key findings and recommendations regarding the implementation of the NFPP and the SLCP. It then presents recommendations to improve and reform critical forest sector policies.

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<sup>1</sup> These findings and recommendations described in much greater detail in the ten case studies, the proceedings of the Workshop on Public Payment Schemes held in Beijing in April 2002, the proceedings of the International Forum on Chinese Forestry Policy held in Beijing in June 2002, as well as the new book entitled *Implementing the National Forest Protection and Land Conversion Programs: Impacts and Lessons*.

## **IMPLEMENTATION OF THE NFPP AND THE SLCP: FINDINGS AND RECOMMENDATIONS**

The Government introduced the NFPP and SLCP to restore natural ecosystems and diminish negative impacts off-site such as flooding, sedimentation of reservoirs, and dust storms. In its second year of operation the Government added to its goals the desire to achieve these environmental objectives in a manner that reduced poverty and contributed to local development.

Task Force studies have found that the two programs have undoubtedly had a huge environmental impact, although the environmental benefits of these programs have not yet been fully evaluated. The logging ban has dramatically reduced exploitation in vast areas of natural forest and the conversion program has planted trees and grasses on hundreds of thousands of hectares of sloping agricultural land. In general, this reduced pressure and new vegetation will help restore ecosystem health, although environmental gains would be enhanced in many cases with better, more ecologically appropriate, land use technologies. In the meantime, the Task Force studies also found the programs have generated a host of unintended, and adverse, social consequences: including dramatic increases in poverty, diminished fiscal incomes, greater tenure insecurity, and accelerated increases in timber imports from other countries.

In the case of the NFPP in particular, and despite the subsidies provided, the impacts on local livelihoods are extensive and, in many cases, severe. Even the state-owned forestry enterprises and their staff, which have received the bulk of the compensation provided by the NFPP, crisis-level impacts are occurring in a many areas. Perhaps most importantly, the logging ban was arbitrarily extended in many areas of the country to collective forests, which since the tenure reforms of the 1980s have become more productive than state-owned forests. Denying these communities the right to benefit from their investments in their forests not only contradicts existing legislation but compounds tenure insecurity and diminishes incentives to invest in forest restoration and management.

Regarding the SLCP, there is no evidence that the SLCP has directly led to increases in poverty, but there is evidence that food subsidies have distorted local markets and put downward pressure on prices, therefore decreasing incomes for farmers who still rely on crop production. In the short term, many local economies might suffer setbacks due to the downsizing of agriculture and its induced decline of agricultural input supply and agricultural product processing industries.

Given these lessons the Task Force recommends the following actions to improve the contributions of the NFPP and the SLCP to government goals of restoring forests and grasslands and improving rural livelihoods:

- NFPP
  - Remove the ban on logging from all collectively-owned forests;
  - Develop a strategy to drop the logging ban from state-owned forests. This ‘exit strategy’ would include a forward-looking plan for restructuring public forest administration, the identification of permanent protected areas and new strategies to conduct sustainable forest management on state-owned forests; and

- In the interim, compensate collective forest holders for losses caused by the ban and increase the level of compensation to those impacted by the logging ban on state-owned forests.
- SLCP
  - Develop a strategy to engage other sector agencies in reducing sedimentation from engineering works;
  - With the active participation of local officials and representatives of stakeholders, improve the targeting and implementation of the program – by adopting specific environmental targeting criteria and more market-based mechanisms such as bidding; and
  - Develop a “sustainability” strategy to continue the positive benefits of the program following the end of the subsidies. This ‘sustainability’ strategy would include an aggressive piloting and advancement of alternative funding sources for these payments for ecosystem services, including a redesigned Ecosystem Compensation Fund and promotion of new markets and payment schemes for carbon sequestration.

## **FINDINGS AND RECOMMENDATIONS FROM POLICY STUDIES**

### **1. Forest Sector Governance and Administration**

*Key Policy Issues.* The forestry sector has lagged behind others in reforming and adjusting to the new market orientation of the government. Field studies and policy analyses demonstrate the need to rethink the role of the government in governing the sector and to adjust the scope of authority of State Forestry Administration accordingly. There are basically two categories of issues: those related to reconsidering how the government manages publicly-owned forests, and that related to how the government guides, monitors and encourages private forest owners and forest enterprises to manage sustainably and develop according to national goals. In the first category, the government needs to restructure public forest management and decentralize state-owned enterprises.

In the second category, the work of the SFA needs to be re-oriented towards guiding, monitoring and regulating private actors and away from implementing investment and development programs. A key to success will be devolving functions to the private sector and decentralizing authority to lower levels of government consistent with the need to ensure that national (i.e. State) forest management and protection objectives can be ensured. Once the goals and strategies of devolution and decentralization are in place, the government will need to organize a coherent strategy to manage these transitions, balancing the interests of the different sectors of society and the needs of the nation.

*Priority Policy Reforms in the Short-Term:*

- Establish one or more multisectoral task force(s), with representatives from key constituencies, to lead the process of restructuring public forest management and the role of the government in guiding private actors. This second task will entail harmonizing bureaucratic structures and decentralizing authority in public forest administration;
- Establish independent systems to monitor and evaluate performance of

- government and private forest managers at different levels
- Set up pilot projects to test institutional innovations in three areas: public forest management; decentralized public administration of private sector forest management; and devolved responsibility from public to private actors.

#### *Priorities for Policy Research*

- Identify innovative decentralization and devolution approaches to manage state forests and govern private sector operations;
- Identify lessons from managing forest sector transitions from other countries;
- Disseminate national and international lessons to debate across all levels of policy making bureaucracy and private sector constituencies;
- Explore options to increase public awareness of forestry policy options and increase private and civil sector participation in policy design, monitoring and setting new standards for the forest sector
- Devise options to rationalize the public forest estate: allocating forest to protected areas and collectives what would be appropriate and devising new institutional arrangements to manage the rest for multiple use by public forest agencies.

## **2. Taxation and Fiscal Policies**

*Key Policy Issues.* Sector performance is now constrained by high levels of taxes – especially as compared to the agricultural sector. In addition, the large number of entities that have authority to tax and the variability of tax levels by year create great uncertainty in the tax burden. Local governments need tax revenues to monitor and regulate the sector, but lower and more predictable levels will greatly improve sector performance. Key issues include identifying what agencies at what levels of government should have authority to set taxes, what the tax levels should be, and how the transition to a new tax regime would be best undertaken.

#### *Priority Policy Reforms in the Short-Term*

- Rationalize taxes, simplifying the system and reducing the uncertainty, yet ensuring that local government costs are adequately financed, accompanied by substantive administrative and regulatory reform.

#### *Priority Policy Research Issues*

- Investigate tax disincentives to allow for competitive forest industry investment and development;
- Study the impact of reduced taxes and deregulation on forest productivity growth and fiscal performance;
- Study the impact of upcoming international and domestic mechanisms of carbon trading on forest investment, ecological protection and poverty alleviation.

## **3. Forest Land Tenure and Ownership**

*Key Policy Issues.* The overall lack of respect of property rights and the divergence between de facto and de jure rights creates uncertainty, discourages investment and undermines respect for the law. The extension of the NFPP to collective forests reverses the gains made by the HRS at a time when the production from those forests is increasingly important to the national timber supply. The many, confused and

overlapping land regulations further discourage efficiencies of land use and the land market. The lack of independent and credible bodies to mediate land disputes and weak judicial institutions are critical constraints to a robust forest sector.

*Priority Policy Reforms in the Short-Term*

- Strengthen property legislation pertaining to collective forests in accordance with the new land contract law, identifying due process for government takings and procedures for valuation and compensation in cases of eminent domain;
- Deregulate controls on private land use, shifting towards a strategy of incentives and payments to ensure the production of publicly valued ecosystem services; and
- Pilot the devolution of forest resource management of state owned forests exploring new arrangements such as household based forest management, management concessions to forest enterprises, auctioning of afforestation projects, harvesting contracts, etc.).

*Priority Policy Research Issues*

- Investigate and develop best practices of internal property rights systems for collective ownerships; and
- Explore different tenure arrangements for state forests and implications on efficiency, productivity and resource use behavior change.

#### **4. Approaches to Regulate Forest Harvesting**

*Key Policy Issues.* The dramatically declining flows of timber from public forests over recent decades and the recent political reaction to ban logging in public forests demonstrate the ineffectiveness of the existing system for setting the annual allowable cut (AAC). Furthermore, the centralized system of setting AAC for all forest jurisdictions in all of China, regardless of ownership, is an unnecessary intrusion on the rights of private and collective forest owners. International experience provides proven options to promote sustained yield on public and private forests without infringing on private rights.

*Priority Policy Reforms in the Short-Term:*

- Eliminate mandated AAC quotas from collective and private forests, limiting quotas to public forests.

*Priority Research Issues*

- Investigate modern methods to set harvest levels on public forests, including an analysis of methods used in major forested countries that have a proven record of sustainable forest management;
- Explore voluntary and regulatory approaches to encourage sustainable forest management on private and collective forests. Approaches used in other countries that merit serious study include the code of harvesting practices from FAO, and the voluntary approaches to encourage the adoption of Best Management Practices in some States in the U.S, among others.

## **5. Forestry and Trade Agreements**

*Key Policy Issues.* Membership in WTO and APEC has potentially dramatic implications for China's forestry sector. The most important issue is not the reduction of tariffs, since they are already low and within the required range, rather the host of rules limiting government authority to subsidize particular sectors. This "second wave" of trade issues has yet to be assessed as they apply to China and the Government has yet to begin to adjust its forest policies accordingly. On the other hand, the importance of the awareness of Chinese government on the impacts of its forest policy change in the world has dramatically increased.

### *Priority Research Issues*

- Assess the implications of WTO/APEC trade liberalization on China's forest industry and existing forest policies;
- Assess the impacts of China's policy change on world market and resource management.

# **The Report**

## **I. Introduction**

The CCICED Western China Forest and Grassland Task Force was established in the summer of 2000, in response to the Government's increased policy emphasis on both forests/grasslands management and on the economic development of Western China. The Task Force has two-year duration. It was approved by the 2<sup>nd</sup> phase of CCICED and extended for the 3<sup>rd</sup> phase of CCICED.

The multi-disciplinary, multi-national Forest and Grasslands Task Force, led by co-chairs Shen Guofang of the Chinese Academy of Engineering and Uma Lele of the World Bank, is intended to support the Government in the ecologically, socially, and economically sustainable development of forests and grasslands in Western China. The Task Force's aim is to identify and address the relevant knowledge, policy, planning, and implementation gaps; integrate and build upon recent and on-going quality work; and to provide independent, quality advice to the State Council, China's highest policy making body, as well as policy makers at other levels.

The Task Force appreciates the opportunity provided by the CCICED to provide an independent evaluation of the National Forest Protection Program and the Land Conversion Program, and to reflect more broadly on opportunities to strengthen the forestry sector. The Task Force applauds the Chinese government's recent efforts to transform the government forest sector from a timber production orientation to one that is dedicated to restoring and conserving forest ecosystems and contributing to sustainable development. The Task Force believes that current programs and financial commitment of government are reflection of government's strong commitment to the ecological restoration of Western China while addressing the complex social income and employment implications for the forest-dependent households. These steps have the potential to establish a foundation for sustainable development in Western China and the Task Force wishes to make a positive contribution to this reform process.

During its first year, the Task Force focused its efforts on the Natural Forest Protection Plan (NFPP, or the "logging ban") and the Land Conversion (to Forests and Grasslands) Program (SLCP). Through a series of ten case studies in nine of western China's Provinces, the Task Force gathered detailed information on implementation of these policies at the local level. As an example of the scale of this work, a total of over 1400 surveys were conducted at the household level alone. Synthesis of the results of the ten case studies generated recommendations on both of the policies; and these were presented to the CCICED at its October 2001 meeting.

Year Two Task Force work built on the results of Year One, but focused on the underlying policy issues revealed by the case studies. This reflects the belief of the Task Force that examination of NFPP and SLCP alone is not sufficient for the long term. Alternatives and solutions for achieving sustainable forest and grassland management in the long term are also needed. Thus, in addition to completion of the work on these policies, Year Two work focused on analysing key policy and technical issues identified in Year One as being fundamental to reforming China's forest and grassland sectors. Work was conducted in a manner that builds constituencies for policy reforms, strengthens China's capacity for policy analysis, and helps establish a basis for future forest/grasslands-related research and policy in China beyond the life of the Task Force.

The scope of Year Two work may be categorized into two areas: (1) assessing the impacts and lessons learned from field studies of the implementation of the NFPP and the SLCP; and (2) conducting new studies of key policy issues underpinning the forestry sector.

Much synergy has been found between the Task Force framework of policy study and the ongoing SFA Study on Sustainable Forestry Development Strategy of China. In particular, the Task Force found its work and findings consistent with SFA's new strategic study to provide a new vision for the forest sector, increasing its contribution to achieving the goal of sustainable development:

- Environmental protection
- Poverty reduction
- Development of national forest industries

## **II. Activities and Products in Phase II**

The Task Force has been active in the following areas: (1) designing, organizing and commissioning thematic studies on ongoing national policies; (2) fostering policy dialogues between researchers and government (decision making and project implementing) agencies; (3) holding high level policy workshops to exchange and disseminate research information and products on critical current policy issues; (4) disseminating research findings through formal publications, policy briefs, newsletters and other fora. This section reviews the key activities and products of Phase II.

### **Policy Dialogue on the Implementation of the NFPP and SLCP**

A technical meeting to review and discuss the findings from the case studies of program implementation was held December 2001 in Kunming. Case study teams met with SFA officials, to report their findings on socio-economic impact of NFPP and SLCP, and to receive feedbacks from the relevant agencies and officials. The discussion was very hot and remarks by SFA officials were positive. The officials were impressed by the household level survey and the rich information generated from the case studies. The case studies, as commented by one official, provided very different information that traditional official survey was not able to generate. The case studies raised concerns that were shared by the officials and other scholars and point out possible solutions that the officials and scholars welcomed.

### **Workshop and Conference**

The Task Force sponsored a workshop and conference with the active participation of a wide array of Chinese and external experts. In the April workshop on public payment schemes, 88 international and domestic participants were present. Domestic participants included Vice Administrator of SFA, DGs of SFA's policy department and several other departments. Many came from provincial level forestry agencies and local universities. As an important follow-up event, SFA and CCAP will co-sponsor a workshop and a training course on international carbon trading at the end of year 2002.

The Task Force sponsored an international conference, entitled the International Forum on Chinese Forestry Policy in June 2001 and both Administer Zhou Shengxian and Vice Administer Zhu Lieke attended. Mr. Zhu came at the first morning and gave a presentation on SFA's ongoing strategic study. Mr. Zhou attended the Forum's conclusion session. After listening to the recommendations by the Task Force representative on Chinese forestry policy, Mr. Zhou provided warm response and delivered a speech on his vision of Chinese forestry development. More than 160 attendees, from both international and domestic, Beijing and local agencies, participated the two day conference and enjoyed hot debate during the meeting.

### **Studies, Expert Investigations and Publications**

The Task Force conducted new forest policy studies on the following topics:

- Forest policy development and implementation for an economy in transition and undergoing restructuring
- The role of the state in the forestry sector
- Forest land tenure

- Forest taxation and fiscal policies,
- Forest resource management and marketing regulations,
- Regional and international impacts of current policy and opportunities

*Expert led investigations.* From April 21 to 30, 2002, Professor Shen Guofang led a team of experts and carried out an investigation of progress in NFPP and SLCP, in Sha'anxi, Ningxia and Gansu. This was the second time that the Task Force had expert team visiting the program sites and re-investigate the ecological, social and economic impacts of the two programs. Recommendations from this survey were presented in the Task Force's June conference, by Professor Shen, and have been incorporated into the Task Force report. A policy brief was published by Chinese Academy of Engineering.

*Publications:*

- Published books socio-economic impact and policy implications of NFPP and SLCP, and the finalized case studies
- Proceedings for the Workshop on public payment schemes, with topics as follows: (1) international experiences with public payment schemes for environmental services; (2) guidelines for monitoring and evaluation in public compensation schemes; and (3) the Chinese Ecological Compensation Fund
- Proceedings for the International Forum on Chinese Forestry Policy, with topics as follows: (1) Forest policy framework for economy under transition; (2) forest and land tenure rights and tenure insecurity of collective forests; (3) impacts of the existing forest resource management system and recommendations for reform; (4) forest tax and fiscal policy options for reform; (5) the role of the state in forest administration and governance; and (6) Chinese forest industry under logging ban and WTO.
- Policy Briefs, Newsletters and Web Site.

*Media Exposure.* The two conferences raised attention among forestry communities and media. They were reported in China Green Times in large volumes. Papers were solicited by journals and newspapers. Some were published in China's "International Economic Review", "Forestry Economics", and "Forestry Science and Technology Management", etc.

### **III. Indicative Impacts of Phase II**

Of the eight recommendations forwarded by CCICED to SFA from the June conference, five of them prepared by the Forest and Grassland Task Force, were paid high attention. SFA assigned thematic study groups for each recommendation to develop understanding and prepare response. A monitoring and evaluation program was under consideration by SFA to improve implementation of NFPP and SLCP, an area of activity that the Task Force has provided very strong inputs. The SLCP Center and the Task Force have co-sponsorship on the newly finished report with regard to improving monitoring and evaluation of SLCP policy. Socio-economic impact and regular-based rural household survey approach will be explored by SLCP Center of SFA, another important area that the Task Force has had pioneered. CCAP has been contacted by SFA to participate in the future socio-economic impact study along the course of the program implementation.

One policy brief has been submitted by the Secretariat of the Task Force to the leader of CAS on how to improve China's ecological benefit compensation system. Policy briefs have also been solicited by SFA to provide updated information with regard to the progress and lessons in the ongoing NFPP and SLCP.

## **IV. Review and Recommendations on NFPP and SLCP**

### **NFPP**

Task Force studies have found that the NFPP has undoubtedly had a huge environmental impact, although the environmental benefits of this program have not yet been fully evaluated. The logging ban has dramatically reduced exploitation in vast areas of natural forest. In general, this reduced pressure will help restore ecosystem health, although environmental gains would be enhanced in many cases with active management aimed at restoring forest ecosystem health.

In the meantime, Task Force studies also found that negative socio-economic impacts are extensive. Even for state-owned forestry enterprises and their staff, which have received the bulk of the compensation provided, crisis-level impacts are occurring in certain cases. Important issues that emerge are the problems with a blanket ban for enterprises that are resource rich, and the question of whether alternative management regimes that allow selective logging may be more appropriate for such enterprises. A blanket ban also rules out possibilities in many places for measures such as health tending and thinning, which are considered important to the health of forests. Another emerging issue is the need for greater attention to diversification initiatives. In terms of local governments and quasi-public provision of public goods and financial services, it appears that, at least in the short-term, local governments that were previously highly dependent on the timber economy will need outside help with their public finances at a greater level than is currently being provided. Finally, impacts on rural households outside the state sector reveal a devastating picture that draws attention to the fact that these stakeholders have not been included in any substantial way in the compensation scheme. Impacts on rural households that previously had access to community forests raise a host of very critical issues with regard to sustainable management regimes and tenure

Key issues limiting program effectiveness and efficiency mostly pertain to inadequate design and targeting and the centralized nature of implementation. For example, studies have shown that engineering infrastructure contributes as much or more to stream sedimentation as does hillside agriculture. Natural forest and grassland regeneration is often much more effective than planting exotic, fast growing trees.

Specific areas of concern include:

1. The Task Force found that funding has not been sufficiently prepared by central and local government, resulting in severe negative social and economic impacts, such as:
  - Lack of compensation for collective forests included in the logging ban;

- Lack of aid for communities in the natural forest areas, leaving the communities suffering economic loss due to loss of economic opportunities.
  - Lack of a system that can help local communities to shift from being forest dependent to alternative economic activities; Establishing appropriate system, such as micro credit, technical assistance, is of necessity.
2. The legal issue of imposing logging ban on collective forests is not resolved. Its impact to reduce private sector incentive to invest in long term forest operations contradicts the goals of the NFPP. Initiatives to remove the logging ban from collective forests, such as is being undertaken in Sichuan, should be encouraged.
  3. Study of best practice in natural forests should be put on agenda. Priority should be given to exploring ways to reform current state own forest enterprises in order to establish a system that work to the objective of sustainable forest management in China. Code of forest harvesting proposed by FAO should be studied and tested in China. Experiences existing in state forest enterprises in alleviating economic burden, raising income for enterprises and employees without degrading forest resources, enhancing efficiency and productivity in forest industry, etc, should be promoted. Experimenting in increasing private sector participation in natural forest management, utilization and investment should be encouraged. Examples include household based forest management responsibility system initiated in Heilongjiang Forest Industry Bureau, auctioning of forest harvest concession (reduced harvesting cost and compliance with harvesting code, etc.), and development of private processing industry in the state owned forest regions, etc. These experiments are promising initiatives that demonstrate optional approaches to manage state forests in sustainable manner.

## **SLCP**

1. Funding for implementation was found insufficient. This inadequate funding, combined with the stringent requirement on quality and timing, created incentives among implementation agencies for lower quality of seedling supply and reduced quality of afforestation work.
2. Task Force studies also found that short-term impact on local economy is negative in many cases, especially in the sectors that provide production inputs and in the sectors that process agricultural products. Regional economies might suffer temporary setback due to the agricultural downsizing. Greater subsidies to alleviate this type of hardship should be in place, together with other arrangements, such as micro credit and extension and training programs.
3. Monitoring and evaluation of the impact of SLCP project in representative areas, to make sure the projects meet the objective of ecological improvement (soil and water conservation), poverty alleviation and economic structure adjustment, should be conducted in a regular basis. Policy adjustment should be made if warranted by information from the appropriately designed monitoring and evaluation process.

4. Tenure issues, after the conversion of agricultural land into tree crops, should be studied carefully in order to ensure the sustainability of the project outcomes.
5. Even if the outcome of land conversion is stabilized, there still exists the possibility of, in the case of price increase and food shortage, the clearing of new land in a different location. This has happened in the pasture area. When pasture land was closed from grazing, herders tend to shift some of the grazing activities to other locations (e.g. from Qinghai to Sichuan). Therefore, implementation of the land conversion program should be conducted in coordination with other programs that aim to generate off-farm employment and restructure rural economies.

## **Recommendations to Improve the NFPP and SLCP**

1. NFPP
  - a. Remove the ban on logging from all collectively-owned forests;
  - b. Develop a strategy to drop the logging ban from state-owned forests. This ‘exit strategy’ would also include a forward-looking plan for restructuring public forest administration, the identification of permanent protected areas and new strategies to conduct sustainable forest management; and
  - c. In the interim, compensate collective forest holders for their losses caused by the ban and increase the level of compensation to those impacted by the logging ban on state-owned forests.
2. SLCP
  - a. Develop a strategy to engage other sector agencies in reducing sedimentation from engineering works;
  - b. Improve the targeting and implementation of the program – by adopting specific environmental targeting criteria and more market-based mechanisms such as bidding, with the active participation of local officials and representatives of stakeholders;
  - c. Develop a “sustainability” strategy to continue the positive benefits of the program following the end of the subsidies. This ‘sustainability’ strategy would include a aggressive piloting and advancement of alternative funding sources for these payments for ecosystem services, including a redesigned Ecosystem Compensation Fund and promotion of new markets and payment schemes for carbon sequestration.

Above all, Task Force research on the NFPP and the SLCP revealed significant weaknesses and gaps in the policy framework necessary for sustained protection and production in the forest and grassland economies, and the inability of government subsidies to override those constraints. Tenure insecurity, high tax rates, subsidies that favour state enterprises over private, and a host of government distortions all diminish land holder incentives to restore their forests and grasslands and manage them in a sustainable manner. Poor public forest management is due to history of incentives to over-harvest – not a lack of subsidies.

## **V. Recommendations to Improve Forest Sector Policy Framework**

The following recommendations are synthesis of three tracks of information:

- (1) Thematic policy studies commissioned by the Task Force;
- (2) International experiences presented by international experts, prepared for the Task Force and its policy workshops;
- (3) Summaries of group discussions from the policy workshops.

### **Policy Development and Implementation for an Economy in Transition**

Chinese economy is under transition toward an increasingly market-oriented system. The society benefits tremendously from the reform for higher economic efficiency, more products, better services, and so on. China's forest sector, on the other hand, has lagged behind in terms of promoting market and grass-root participation. Consequently, forest sector may miss the opportunity to benefit from increased demand and trade liberalization.

Achieving the goals of environmental protection and improved rural livelihoods will require urgent attention to those fundamental policy constraints that distort the incentives of both public and private land managers. Looking deeper, Task Force studies reveal a concept of the role of the state centered on redistribution of resources and direct control over land use regardless of ownership. This concept not only contradicts existing law—as it pertains to private and collective landholders—but is out of step with modernization reforms in other sectors of the economy and the stated aspirations of the government.

Reform in China's forest sector has moved the farthest on collective forest tenure change with an iterative process. In forest resource management system, and in China's state owned forest areas, reforms are relatively slow.

To establish a sustainable forest sector, there is a need for a coherent policy framework. This framework should avoid any conflict among different forest policies, and should avoid conflicts between policies made for forestry and policies made for other sector (i.e. Law of Grassland, Water and Soil Conservation Law, and Forest Law, etc..)

Based on international experiences and domestic lessons, there is also an urgent need to coordinate actions among different sectors. There should be some recognition that policy change outside the forest sector might have bigger impact on forestry sector policy. On the other hand, when forest sector is taking on bigger responsibility now than before, it should recognize the value of existing experiences, lessons and scientific knowledge accumulated from other relevant sectors. Currently there is no mechanism to systematically and independently learn from the lessons of experience and reflect them in finetuning policy or implementation. A mechanism (Task Force) that facilitates exchange of knowledge and coordinate acts between sectors would greatly reduce the chance of failure and shorten time of learning.

While existing forestry problems call for a systematic reform in China's forest sector, there is no readily available model in the world that can be directly borrowed. However, learning from international experiences is still very important. Studying what already exist and tried out in forest areas by forest farmers, rural communities, and state owned

forest enterprises is also very important and is the only way to find direction for future policy reform.

## **Governance and Administration of the Forest Sector**

Field studies and policy analyses demonstrate the need to rethink the role of the government in governing the sector and to adjust the scope of authority of State Forestry Administration accordingly. There are basically two categories of issues: those related to reconsidering how the government manages publicly-owned forests, and that related to how the government guides, monitors and encourages private forest owners and forest enterprises to manage sustainably and develop according to national goals. In the first category, the government needs to restructure public forest management and decentralize state-owned enterprises.

In the second category, the work of the SFA needs to be re-oriented towards guiding, monitoring and regulating private actors and away from implementing investment and development programs. A key to success will be devolving functions to the private sector and decentralizing authority to lower levels of government consistent with the need to ensure that national (i.e. State) forest management and protection objectives can be ensured. Once the goals and strategies of devolution and decentralization are in place, the government will need to organize a coherent strategy to manage these transitions, balancing the interests of the different sectors of society and the needs of the nation.

The transformation of forest sector's focus from marketable products (timber, etc.) to ecological services should not lead to a bigger forest administration and wider scope of government intervention in forest management.

The stated 6 major programs at SFA will help the forest authority to be more focused and maybe more effective in achieving its set goal of ecological improvement in the near future, but this newly set focus should not be used to compete away financial resources otherwise available for the private sector.

In many areas the private market is more effective and cost efficient than governments even in supplying public goods. Bidding and auctioning approach proved in many sectors to be effective to ensure cost efficiency and maintain high quality. They should be used in the implementation of key forest projects, in the area of afforestation, road construction, inputs supply as well as harvest concession.

Not only a bidding and auctioning system should be in place, but also a wide array of entities should be allowed to participate in the design, implementation and management of forest project. Of the entities, rural communities should be given opportunity and authority in participating in the decision making process and their property right over local forests should be secured and enhanced, and their customary rights over local natural resources should be respected.

An independent system of monitoring and evaluation should also be a priority in order to reduce management cost and increase effectiveness of project implementation.

### *Priority Policy Reforms in the Short-Term:*

- Establish one or more multisectoral task force(s), with representatives from key

constituencies, to lead the process of restructuring public forest management and the role of the government in guiding private actors. This second task will entail harmonizing bureaucratic structures and decentralizing authority in public forest administration;

- Establish independent systems to monitor and evaluate performance of government and private forest managers at different levels
- Set up pilot projects to test institutional innovations in three areas: public forest management; decentralized public administration of private sector forest management; and devolved responsibility from public to private actors.

#### *Priorities for Policy Research*

- Identify innovative decentralization and devolution approaches to manage state forests and govern private sector operations;
- Identify lessons from managing forest sector transitions from other countries;
- Disseminate national and international lessons to debate across all levels of policy making bureaucracy and private sector constituencies;
- Explore options to increase public awareness of forestry policy options and increase private and civil sector participation in policy design, monitoring and setting new standards for the forest sector
- Devise options to rationalize the public forest estate: allocating forest to protected areas and collectives what would be appropriate and devising new institutional arrangements to manage the rest for multiple use by public forest agencies.

#### **Taxation and Fiscal Policy**

Unreasonably high taxation is common knowledge in China's forest sector. In China's collective forest area, tax distortion is even more serious, taking up 40-70% of the timber sales. There is no argument that this significantly reduces commercial timber sector's comparative advantage and places huge disincentive to forest investment, something that works against the main goal of forest sector in China.

Large taxes and fees are not without its institutional basis. China maintains heavy regulations over forest resource management and utilization, even in what has been classified as collectively owned forests. On the other hand, forest projects still remain largely government action. These activities require a large forest administrative force. However, budget to feed this large force is far from sufficient. The need to maintain the large administrative force creates needs for increasingly higher taxes and charges over timber sales.

This being known, taxation reform has to start with institutional reform. Downsizing government direct project, reducing regulatory distortion hence the need for large administrative force is the key to reduce the tax and fee distortion.

As for the fiscal policy, the allocation and use of program funding and the performance of forest program can be improved when objective, independent monitoring and evaluation mechanism is established. The M&E system should be run by teams outside the implementation agency and should target more on the social and economic aspect of the project implementation.

New opportunities, such as Carbon Trading mechanism, should be paid bigger attention. In the future, participating in carbon trading can potentially earn Chinese forest sector tremendous amount of credit and consequently large financial in-flow. Proper utilization of the mechanism will greatly enhance forest sector's financial performance, therefore enhance the incentives of forest producers for more investment and better management.

#### *Priority Policy Reforms in the Short-Term*

- Rationalize taxes, simplifying the system and reducing the uncertainty, yet ensuring that local government costs are adequately financed, accompanied by substantive administrative and regulatory reform.

#### *Priority Policy Research Issues*

- Investigate tax disincentives to allow for competitive forest industry investment and development;
- Study the impact of reduced taxes and deregulation on forest productivity growth and fiscal performance;
- Study the impact of upcoming international and domestic mechanisms of carbon trading on forest investment, ecological protection and poverty alleviation.

### **Forest Land Tenure and Ownership**

Stability, predictability and consistency in the de jure and de facto land tenure and transparency in its implementation is critical. Forest land tenure reform has been very active. Land tenure arrangement varies significantly across regions and over time. The success of the land tenure reform also varies.

Forestland tenure reform, mainly decentralization of collective forests, was mostly influenced by the Household Production Responsibility System (HPRS), adopted by the agricultural sector in early eighties. Counterpart reform in the state forest areas, like household based natural forest management and agricultural land contracting system inside state forests, has also been attributed to HPRS influence. It is conceivable that future forestland tenure reform will still follow the lead of rural agricultural reform.

The active forestland reform contributed greatly to the formation of current forest landscape. When investment is available, productivity of afforestation projects is much higher, which explains China's recent success in plantation development and give the government confidence in its grand ecological projects. On the other hand, the rapid growth of economic forests, bamboo forests are also consequences of the increased land use rights by farmers due to the tenure reform.

What separate forest sector from the others is the importance of tenure security. Tenure insecurity will increase the risk of forest operation, therefore imposing disincentive for rural households and private investors to commit long term resources in forestland management. China's experience is a prove of it. Although forestland tenure is being constantly decentralized, in many places it is subject to administration's will for adjustment. Existing harvesting regulation and market distortion compound the negative effect. The consequences are: farmers have very little incentive to invest in afforestation and reforestation, especially in those of ecological importance. Farmers are more inclined to plant economic forest crops, bamboo forests, and cropland, which give farmers short term benefit but may not fit the government's goal of ecological protection.

There is tremendous need for a legal framework to secure tenure: to avoid administrative intervention in forest use and violation of tenure arrangement, customary rights, etc. and depriving of use right (i.e. logging ban).

While logging ban in natural forest is clearly beneficial for the rehabilitation of the depleted natural forest ecosystem, extension of the ban into collective forest areas, not only is a violation of collective forest tenure rights, but also a huge blow to the development of forest resources in the collectively owned forestland.

In NFPP, property rights of collective forest owners must be respected and protected. Compulsory shutting down of farmers' production activities in collective forests are in principle against forest law and should be reversed, unless reasonable compensation was provided. Logging ban in collective forests damages farmers ' and private sectors' trust toward government policy, causing disincentive to invest in forestry, therefore should be lifted immediately or a compensation mechanism has to be established immediately..

In the forest areas with marginal ecological significance, tenure rights should be granted to local community and rural household from state sector (state farms, enterprises) for better management and to increase economic situation of the local community. There are trials in the state forest enterprises in contracting out forest management right to workers family. The recent observations are that certain experiments create opportunities for workers to generate greater income from managing non-timber forest products. The trials also show promising trend in behaviour change in terms of resource use and provide possible solution for transforming state forest industry into an efficient and sustainable sector. The experiences should be closely examined.

#### *Priority Policy Reforms in the Short-Term*

- Strengthen property legislation pertaining to collective forests in accordance with the new land contract law, identifying due process for government takings and procedures for valuation and compensation in cases of imminent domain;
- Eliminate compulsory land use changes and deregulate controls on private land use, shifting towards a strategy of incentives and payments to ensure the production of publicly valued ecosystem services; and
- Pilot the devolution of forest resource management of state owned forests exploring new arrangements such as household based forest management, management concessions to forest enterprises, auctioning of afforestation projects, harvesting contracts, etc.).

#### *Priority Policy Research Issues*

- Investigate and develop best practices of internal property rights systems for collective ownerships; and
- Explore different tenure arrangements for state forests and implications on efficiency, productivity and resource use behavior change.

### **Regulation of Forest Harvesting**

Chinese government uses harvesting quota and logging ban to control timber production. The main purpose of these regulations has been to prevent existing forest resources from declining. The expectation is, timber harvest regulation together with government's

increasing investment in afforestation, would achieve the goal of stabilizing and expanding China's forest resources.

The harvesting quota system was established in Forest Law 1984, but officially put into practice in 1987. The principle of the system is the volume of timber harvest can only be set below the volume of timber growth. It is the central forestry authority to set the national table of harvesting quota for all regions and provinces. Provincial level forestry authorities then redistribute the quota to subordinate regions, so on and so forth.

The global experiences indicate that harvesting quota system, or what is conventionally called annual allowable cut system, is implemented where the state and government have property rights. It is more often applied to the protected forests under public ownership. Private forest owners should have rights to decide when, how and how much to cut and utilize their own forests. When the state has stake in the forests under non-state management, the benefit sharing system should be established. Once private forests are required to provide public services, a reasonable compensation scheme should be in place.

Where the logging quota system is enforced, it imposes restriction to the ability of forest producer to generate maximum economic return from their operations, therefore damages producers' incentive to re-invest in the forests. The consequences include declining quality of existing forests due to inadequate maintenance, conversion of forestland into cropland and other more economically viable land use, and insufficient private investment in reforestation and afforestation. The implementation of logging ban in China's state owned natural forest areas proves the failure of current yield regulation system including logging quota.

For the last several decades, there are a number of countries adopting practices of logging ban. This global experience indicates that logging bans are relatively ineffective instruments for maintaining/improving conservation/environmental values; they have been shown to have had negative social and economic consequences in China in the absence of alternative strategies for compensation and wood supply. The farmers running private forest operations inside the logging ban areas and the rural communities living around state owned forests suffer the most setback in economic term, due to downsizing of the timber economy. These setback encountered by the rural communities have been neglected in the compensation policy. On the other hand, neighbouring countries face tremendous threat of deforestation due to China's increased domestic demand after logging ban.

The Task Force strongly recommend that an exit strategy to replace logging bans with harvest allowable under sustainable forest management regimes is a high priority. While the logging ban provides opportunity for state owned forest enterprises to rearrange their operation and employment, it is important to utilize the opportunity to explore new regimes in afforestation, forest management, forest resource harvesting, processing and marketing. Experiences accumulated in the past when these enterprises suffered severe economic hardship but managed to survive should be studied.

Institutional innovations in state forest enterprises include decentralized forest management, auctioning of harvesting and afforestation, development of joint or private processing facilities, etc. The innovations resulted in higher efficiency of forest

operations, higher productivity of forest management and use, and higher income for forestry employees. They should be thoroughly studied, further experimented and promoted. Furthermore, the centralized system of setting AAC for all forest jurisdictions in all of China, regardless of ownership, is an unnecessary intrusion on the rights of private and collective forest owners. International experience provides proven options to promote sustained yield on public and private forests without infringing on private rights.

*Priority Policy Reforms in the Short-Term:*

- Eliminate mandated AAC quotas from collective and private forests, limiting quotas to public forests; and
- Initiate projects in representative forest areas of the country to determine the discrepancy between official forest inventory statistics and reality.

*Priority Research Issues*

- Investigate modern methods to set harvest levels on public forests, including an analysis of methods used in major forested countries that have a proven record of sustainable forest management;
- Explore voluntary and regulatory approaches to encourage sustainable forest management on private and collective forests. Approaches used in other countries that merit serious study include the code of harvesting practices from FAO, and the voluntary approaches to encourage the adoption of Best Management Practices in some States in the U.S, among others.

## **Forestry and Trade Agreements**

Membership in WTO and APEC has potentially dramatic implications for China's forestry sector. The most important issue is not the reduction of tariffs, since they are already low and within the required range, rather the host of rules limiting government authority to subsidize particular sectors. This "second wave" of trade issues has yet to be assessed as they apply to China and the Government has yet to begin to adjust its forest policies accordingly. On the other hand, the importance of the awareness of Chinese government on the impacts of its forest policy change in the world has dramatically increased.

*Priority Research Issues*

- Assess the implications of WTO/APEC trade liberalization on China's forest industry and existing forest policies;
- Assess the impacts of China's policy change on world market and resource management.

## **VI. Conclusion**

The CCICED has been a unique mechanism that cannot be found anywhere in the world. It facilitates conversations between sectors, disciplines and countries and provides Chinese government with timely, objective and high quality information to support its decision in developing Chinese society in a sustainable way.

Members of the Task Force on Forest and Grassland are proud of the opportunity they have been given to contribute to the course of sustainable development of China, particularly Western China. Under the leadership of CCICED secretariat, Co-chairs Professor Shen Guofang and Dr. Uma Lele, the Task Force members worked diligently for over two years. To its satisfaction, the Task Force has been able to generate timely and objective information to evaluate the social and economic impacts of ongoing government programs and policies, and provides recommendations to improve the program implementation. Along the course achievements have been made in the areas of dialogue between academia and government agency, the awareness of the importance of independent monitoring and evaluation system, opportunities for improving ecological compensation system, etc.

There are still large room to improve program implementation and policy development. Attention should be given to the socio-economic impacts of government programs and policy change. An independent monitoring and evaluation system should be in place. Market instruments should be introduced into more aspects of the government program implementation. A system of secured tenure rights in forests should be high priority in the future policy development.

Improvement in policy design, implementation and analysis depends on improvement in capacity. Capacity building at all levels of government agencies and research institutions should be given high attention. Building up strong and independent policy research institutions seem to be particularly important at current time in China.

There is also large gap in the Task Force's work and in the society's understanding of grassland restoration and sustainability. The Task Force notices that the government has made several major policy changes to improve grassland management. Nevertheless, scientific studies and sound policy research in sustainable grassland utilization and management remain insufficient. This Task Force strongly recommends continuation of CCICED's support in grassland study and perhaps an establishment of a Task Force on Sustainable Grassland Management.

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