

AIDE MEMOIRE
Second Joint Mission, 12 – 16 December 2011

Indonesia: Forest Investment Program (FIP)

I. INTRODUCTION

1. Indonesia is one of the eight pilot countries selected worldwide for participation in the Forest Investment Program (FIP), a targeted program under the Climate Investment Funds (CIF). The notional funding resource envelope for FIP in Indonesia is up to \$70 million, including up to \$37.5 million in the form of grant assistance, and up to \$32.5 million as concessional finance. An additional complementary grant pool of about \$6.5 million will be made available through the FIP Dedicated Grant Mechanism for Indigenous Peoples and Local Communities. Implementation of the FIP Investment Plan (IP) in Indonesia is to be jointly supported by three multilateral development banks (MDBs) – the Asian Development Bank (ADB), the International Finance Corporation (IFC) and the World Bank (WB) – with participation and possible co-financing from other development partners.

2. A Preparation Grant of \$225,000 administered by ADB on behalf of the Government of Indonesia (GOI) was approved in January 2011 to assist the GOI in preparing for and conducting joint missions, including development of the FIP IP through a stakeholder consultation process. The First Joint Mission, held from 13 to 22 July 2011, reviewed the information compiled by GOI supported by consultants working under the preparation grant, and identified an initial set of cross-cutting issues to be addressed by the FIP IP in support of Indonesia's emerging National REDD+ Strategy. The Mission conducted field visits in Central Java, Yogyakarta, Jambi and West Kalimantan provinces to identify potential opportunities for FIP investments relevant to REDD+. The choice of locations for the field visits does not necessarily determine the final areas of engagement.

3. The First Joint Mission identified the following eight preliminary areas for further consideration.

- a) **REDD+ in Community Forestry:** Promotion of community forestry (Village Forest/HD, Community Forest/HKM, Private Forest/HR, People's Plantation Forest/HTR), including the prospects for reforming the \$300+ million support fund (BLU), improved credit systems, access to REDD+ performance-based payments, forest carbon markets, and payment for ecosystem services.
- b) **Land and Forest Tenure Reform,** including policy reforms to improve enabling conditions for Sustainable Forest Management (SFM): Forest land tenure, dealing with tenurial clarifications, where multiple claims can hinder REDD+ investment and implementation; and prospects for scaling up tenurial clarification and adjudication systems that can serve as a platform for improved SFM and access to REDD+ financing.
- c) **Addressing Illegal Logging and Associated Trade:** Addressing the remaining hot spots for illegal logging, including the introduction of policy and institutional reforms, and introducing REDD+ incentives as alternatives to illegal behavior.

- d) **Forest Management Units (FMUs) and REDD+:** Supporting the development of FMUs using REDD+ as a management objective and FMUs as potential REDD+ monitoring units, to introduce ecosystem-based innovations for improved land, watershed and forest management.
- e) **Degraded Lands Development:** Redirecting plantations from forests to degraded lands in conjunction with implementation of the national REDD+ strategy.
- f) **Ecosystem Restoration Concessions and REDD+:** Scaling-up the use of Ecosystem Restoration Concessions, with an emphasis on generating REDD+ revenues as an important source of finance for sustainable forest ecosystem management and rural development.
- g) **Market-based REDD+ Incentives:** Laying the groundwork for use of REDD+ financial incentives to reshape land and forest management practices, including the integration of REDD+ into fiscal policy incentives to enable trillions of Rupiah of reflow from natural resource taxes/royalties to affect decision making in provinces and districts.
- h) **Sub-national REDD+ Development:** Testing and developing REDD+ systems and approaches at the sub-national (provincial and district) level in targeted pilot provinces or demonstration locations to link with emerging national institutions and policies, as prioritized by GOI REDD+ agencies, especially where the MDBs have track records or where FIP can serve as the lead partner program.

4. Subsequent to the First Joint Mission, several follow-up meetings were held to review progress achieved in developing the FIP IP and to clarify the process towards delivery. Additional FIP meetings were held using a range of avenues, but the main engagement mechanism has been through Indonesia's National Forest Council (DKN) and outreach to its various chapters covering civil society, the private sector and academia. Meetings with DKN were held on 21 November and 8-9 December where the eight preliminary areas and the basic structure of the DGM could be discussed. Valuable contributions were received and the FIP is open for further inputs, as promised by a number of representatives at the meetings. A number of individual meetings with development partners has also been conducted during this time. The Second Joint Mission¹ was held from 12 to 16 December 2011 to synthesize the information collected and feedback received from various outreach efforts and to refine thinking on key investment options to be pursued under FIP in Indonesia.

5. The mission appreciates the leadership provided by various GOI institutions, and thanks all other stakeholders (national and provincial institutions, and representatives of civil society, private sector, and the development partners) for their support and cooperation. The mission wishes to specifically thank the staff of Ministry of Forestry, the DKN and the Jakarta offices of ADB, IFC and the WB for their assistance and facilitation services provided during the mission.

¹ The Joint Mission comprised: Singgih Riphath (co-team leader, MOF); Hadi Pasaribu (co-team leader, MoFr); Ancha Srinivasan (co-team leader and Principal Climate Change Specialist, ADB); Werner Kornexl (co-team leader and Senior Climate Change Specialist, World Bank); Michael Brady (co-team leader and Forest Program Manager, IFC); *GOI*: Agus Sarsito, Teguh Rahardjo; *ADB*: David McCauley, Mohammed Nasimul Islam; Pantja Putih Wardani; *World Bank*: Tim Brown; Emile Jurgens; Eri Indrawan; Juan Martinez, Guntur Prabowo, Paul Lemaistre; *IFC*: Steve Gretzinger; Haru Ohtsuka; Haris Iskandar; Rahajeng Pratiwi; *Consultants*: Agus Setyarso, Budi Prati, Rowena Crispina Soriaga.

II. JOINT MISSION ACTIVITIES AND KEY FINDINGS

A. Consultation Process

6. Prior to the mission, the Indonesia FIP concept documents and information on the Joint Mission dates were disseminated through both the CIF and DKN web sites. Several information sharing and consultation meetings were held both prior to and during the second Joint Mission. Stakeholder perspectives on how best the FIP design can address drivers of deforestation and forest degradation were obtained through individual and group consultation meetings. In all meetings, the Mission encouraged participants to send their additional comments to an e-mail address - indonesia.fip@gmail.com. The discussions involved a variety of stakeholders – government, civil society, private sector and development partners – as described below.

B. Meeting with Government Ministries and Agencies

7. The mission presented the concept of FIP and discussed in detail the eight initial ideas and the feedback received from the DKN meetings. The government representatives noted that all concepts presented are of high relevance, and they added further ideas, such as the need for addressing oil palm and mining licensing practices, focus on peat fire prevention and erosion, and programs to facilitate investment by reducing institutional, information and implementation risks and barriers. Many participants noted that land tenure reforms and institutional strengthening represent the most transformational investments that FIP can promote. Representative from BAPPENAS stressed the importance of prioritizing KPH as an entry point for other interventions such as ecosystem restoration, REDD+ incentives and sub-national REDD+ development. Legality of timber trade, creation of centralized forest market price data management systems were also stressed as additional areas of focus. Some stakeholders sought additional information on the types of financing that the FIP will provide.

8. The mission clarified that the MDBs would work on the most transformational ideas presented and would support selected ideas based on their comparative strengths and potential for cooperation with other development partners and co-funding prospects. The Mission also discussed the different funding modalities, and specifically on principles of financing through concessional finance. Participants were referred to the decision taken at the First Joint Mission that the concessional finance will go directly to the private sector, without creating any liability for the government and civil society.

C. Meeting with Civil Society

9. Civil society representatives inquired about: (i) the scope for adding new ideas to the eight early ideas; (ii) the financing instruments (grants, loans, guarantees) that will apply to the eight ideas, as well as criteria and indicators for awarding grants and loans; (iii) the timeline between the second mission and full implementation of FIP projects; (iv) the roles expected of civil society organizations (CSO) - including indigenous peoples' organizations – and the process for submitting proposals from CSOs who want to participate; and, (v) safeguards to be applied. CSO representatives also queried if FIP would focus on non-forest emissions (agriculture, mining, palm oil plantations, etc.). The CSO representatives provided feedback on issues such as: (i) REDD+ and Community Forestry; (ii) Land and Forest Tenure Reform; (iii) Forest Management Units; and, (iv) Ecosystem Restoration Concessions and REDD+. Representatives from AMAN mentioned that they would support the FIP Investment Plan by

following a request from FIP Focal Point of the Ministry of Forestry to submit specific comments and recommendations for the plan on the land and forest tenure reform to the FIP Indonesia email address by early January 2012.

10. The Joint Mission clarified that: (i) FIP must be viewed more as catalyst due to the small scale of funds relative to the large needs in Indonesia. Since FIP is not at a scale to attempt all ideas nationwide, comparative strengths of each MDB would need to be considered in relation to country needs; The Mission noted that in general, policy issues will be handled by World Bank and ADB since they have the institutional mandate and experience to do so, whereas the IFC focus would be on the building of the business case for sustainable forestry via on-the-ground implementation with Community Forest Management Enterprises and other members of the value chain. (ii) Grants would be applicable for public sector activities, and financing for private sector activities. Public sector investments on the ground are likely to be at district and provincial levels, coupled with technical assistance for national and sub-national institutions. Concessional finance to the private sector will also be complemented with technical assistance to improve performance; (iii) Long preparation process for FIP in Indonesia relative to other countries takes into account the size of the country, the huge number and diversity of actors, and high complexity of issues. The FIP IP is targeted for presentation for endorsement by the FIP Sub-Committee meeting in April/May 2012. More detailed design of projects to implement the investment plan will commence after IP endorsement; (iv) The role of CSOs in FIP is important not only in early guidance and design, but also in implementation. Depending on certain areas or themes, NGOs with capacity in priority areas or themes can potentially receive funding for technical implementation, since NGOs have an executing capacity on the ground. In addition, the Dedicated Grant Mechanism for indigenous peoples and local communities of around \$6.5M provides space to potentially invite micro-level proposals to help IP groups + local communities prepare for future climate regime; (v) The safeguards procedures of respective MDBs will apply in the site/s where the MDB will operate, as set out in the FIP Design Document. (vi) FIP could focus on drivers of deforestation both within and outside the forestry sector but the actual interventions would depend on resources available.

11. The Joint Mission thanked CSOs for their excellent inputs on issues such as need for paying attention to conflict resolution, institutional strengthening, effective stakeholder participation, effective technical assistance from local banking sector in preparing sound business plans, need for paradigm shift from timber-based utilization to resource-based utilization, need for focusing on restoration of forests on mineral soils besides those on peat lands, and the need for building on the existing 44 pilot projects.

D. Meeting with the Private Sector

12. The Joint Mission met with representatives of the private sector, which included upstream and downstream forestry companies and concessionaires, industry associations, international NGOs working on private sector sponsored projects, management consultants with sector expertise, and local banks with natural resource investments. The private sector supported the FIP process and recognized its importance in providing transformational investments and inquired about (i) criteria to be used to select partner enterprises for financial support, (ii) possibilities for using FIP financing for existing businesses such as industrial plantations (HPH) and natural forestry (HPH) (iii) a realistic timeline for the delivery of the FIP private sector concessional financing, citing concerns on cash flow affecting businesses, (iv) possibilities for using FIP funds as a market guarantee to fund forest carbon credits, (v) the eligibility of projects very far along in the process for funding, (vi) prospects for one district or

province that supports ERCs to receive support in promoting them via the FIP funding. Some representatives asked if working capital can be included in the FIP concessional financing.

13. The Mission replied that all ideas and forestry subsectors would be considered for possible interventions and investment, particularly those that could demonstrate investment leveraging and links, or substantial benefits to small forest enterprises. Regarding investment timelines, the Mission noted that this would depend on the project, but a realistic timeline would be a maximum of 6 months for project funding following the anticipated Country Investment Plan endorsement in April 2012. The Mission noted the possibility to fast-track project development for concessional financing to present together with the Implementation Plan in response to donor enthusiasm for rapid allocation of such financing and spurring private sector transformation and investment as soon as possible. The Mission also noted that working capital is not usually included in FIP investments, but clarified that FIP funds may provide for a longer grace period, lower rates, simpler guarantees and extended payback periods compared to what the financial markets usually provide (depending on market, country, business model, local bank charges, etc). The Joint Mission noted that – within the context of investment contributing to the overall FIP Investment Plan objectives – each MDB has its own performance standards and safeguards in place, and that these will be used to evaluate potential participation, in consultation with the Government.

E. Meeting with Development Partners

14. Several development partners stressed the importance of effective coordination at all levels among REDD+ initiatives supported by both bilateral and multilateral development partners, and in aligning FIP with the National REDD+ Strategy especially during implementation. They recommended that FIP should (i) focus on land tenure issues and high priority provinces in order to obtain a real transformative impact; (ii) add value by exploring transformative change at different scales (national and sub-national approaches); and (iii) sharpen the scope and focus of activities as much as possible to maximize impact considering the limited funding available. They noted that the criteria for selecting projects should be those that can drive the most transformative change. The development partners also advised the Mission to engage the private sector as much as possible, and stressed the need to strengthen local institutions. The BAPPENAS representative noted that focused support to FMUs through FIP will help to build local capacities, ensure monitoring in remote areas, and promote local level management of forest land.

15. The mission thanked the development partners for their inputs and agreed on the need to coordinate its efforts and focus potential interventions on areas that will maximize transformational impact. The Joint Mission agreed to keep communication channels open in order to update each other on the progress of ongoing bilateral and multilateral initiatives, avoid overlapping activities, and ensure time and cost efficiency.

F. National Workshop

16. Participants included representatives from ministries, national institutions, civil society, private sector, development partners, and research institutes. The workshop included presentations on the FIP background and principles, the eight early ideas, and synthesis of feedback received from the consultation meetings prior to and during the second mission. Several participants expressed appreciation of the efforts of the Joint mission for posting relevant documents on the CIF and DKN web sites. Some participants stressed the need for close coordination of FIP with other ongoing and planned initiatives in order to leverage

additional resources. The US Millennium Challenge Corporation's initiative was cited as an example, mainly due to its large budget and possibilities to leverage the FIP investment. The need for building on progress made by other projects such as the Nature Conservancy project in Berau and PNPM program by the World Bank was also noted. FIP support was recommended to help strengthen Forest Management Units or KPH. Other areas of support mentioned included: land tenure reform; food security possibly competing with afforestation in densely populated Java; barriers for promoting ecosystem restoration activities; improving the financial incentives and viability of SFM in production forestry; and creating revenues from protecting and managing for production standing forests and restoring degraded forest lands.. Representatives of research institutions noted that FIP interventions could (i) take advantage of studies on bamboo garden concepts, Nyamplung (*Calophyllum inophyllum*) for bio-energy alternatives and food security, micro-hydro concept for upland conservation activities, forest carbon accounting systems, and (ii) draw lessons from village forest concession processes currently underway. Several participants inquired if FIP will provide technical and financial support for Community Forestry schemes (*i.e.* HTR, HR, HKM, HD, *etc.*).

17. Participants provided feedback on each of the eight ideas presented at the meeting. Some participants stressed that a transparent and easily accessible mechanism to negotiate and resolve land tenure conflicts through strengthening governance and enforcement at the local level is important. Some participants appreciated the possible assistance in the implementation of the decree on timber legality but advised to ensure overlaps with other initiatives. Insofar as FMUs are concerned, some participants suggested that development, implementation and oversight of forest management plans should be done in a participatory way with relevant communities to increase community ownership and improve sustainability of the forest management plans. Some participants suggested that there focus on smallholders should be strengthened with regard to interventions on ecosystem restoration concessions. Some participants noted that details on some interventions such as Market-based REDD+ incentives are still lacking and that further thinking is necessary on the types of activities to be supported through FIP under this initiative.

18. The Mission thanked the participants for their extensive and excellent inputs, and stressed that effective coordination at all levels would be attempted. The Mission acknowledged the need for better coordination of the consultations and increased time allocation. The Mission noted that decisions on concessionality and scope of activities would be made on a project-by-project basis, and that policies on safeguards would follow respective MDB procedures in close consultation with counterpart government agencies. The Mission stressed that while community forestry will be a strong feature of the Indonesia IP, the role of the private industrial sector should not be ignored since it plays a key role in the value chain and has the ability to mobilize large quantities of financial resources. The IP will engage both public and private sector interventions and investments. Insofar as the private sector investments are concerned, they will likely include a range of small, medium and large forest enterprises on private and public lands (plantation owners, concessionaires, cooperatives, small and medium businesses, forest contractors, *etc.*), which are often constrained by weak business capacity, limited access to finance and lack of information on the downstream value chain of the sector.

G. Priority investments for FIP support

19. Based on the stakeholder consultations, the Joint Mission felt that a programmatic approach encompassing three elements should be considered in formulating the IP: (i) national level governance, policy and institutional strengthening for sustainable forest management and the ability to capitalize on REDD+ opportunities, including capacity building, knowledge

management and strategic coordination of FIP investments with related GOI initiatives, including the Indonesia UNREDD and FCPF; (ii) on-the-ground public sector investments, especially in selected provinces targeted by the National REDD+ Strategy; and (iii) strengthening the productive capacities and business skills of small, medium and large forest enterprises, with particular focus on smallholders and communities, and key members of the related value chain by leveraging private sector investments. Considering the different comparative advantages of MDBs the Mission considered three different groups of interventions.

20. The first group of interventions is aimed at exploring the interface between development and diffusion of improved models for community-focused forest management and the ability to tap REDD+ financing. With co-financing from ADB, the Global Environment Facility and Japan, the concept of pro-poor REDD+ investments will be tested at the provincial and district levels through the project “Community-Focused Investments to Address Deforestation and Forest Degradation (CFIADD+) in West Kalimantan”. At the provincial level, CFIADD+ will support the West Kalimantan Provincial Government in developing a provincial REDD+ strategy within the broader context of an economic growth plan that is based on the sustainable management of the province’s land, water and forest resources. This will include development of an overall strategy to address the key drivers of deforestation and forest degradation in the province, including land tenure issues and the illegal trade in forest products. Capacity building activities organized through the provincial component will support work at both the provincial and district levels, with links formed to transboundary forest eco-region management efforts under the Heart of Borneo Program. At the district level, support will be provided to provincial planning by the preparation of more detailed spatial and land-use plans for selected districts such as Sintang and Melawi. In addition, and working through the Directorate General for Forest Protection and Nature Conservation and District Forest Services, support will be provided at the district level for a range of community-focused pilots to address drivers of deforestation and forest degradation, including economic activities utilizing degraded lands for sustainable community livelihoods. To the extent possible, both provincial and district level activities will support development of Forest Management Units as key entry points. A district-wide Safeguards Information System and gender-sensitive benefit sharing arrangements will also be developed. In support of the provincial and district level investments, technical assistance especially with regard to harmonization of national and sub-national policies on carbon stock improvement and creation of enabling environment to leverage additional REDD+ financing will be provided at the national level. In summary, the transformational impacts will be achieved through strengthening institutions and policies, and by bringing about changes in behavior of actors catalyzed through application of modern technologies. Some effort will also be directed at knowledge management and exchange between districts, provinces and countries.

21. The second group of interventions is aimed at reducing GHG emissions by promoting sustainable peat management through (i) improvement of community land use planning processes and livelihood improvements and (ii) through capacity building of local stakeholders, including local communities, Indigenous Peoples and women; and institutions to prepare them for sustainable community forest management, land tenure clarification processes and micro-spatial planning. These interventions are based on the livelihood, tenurial and community development needs. The preparation and support to relevant district institutions (KPH, district institutions, etc.) will be in response to those needs. The intervention will cooperate with local programs and build on ongoing activities and existing community structures and processes at a local level. It would also cooperate with provincial and national institutions to link into the National REDD+ Strategy and into national programs, such as PNPM.

22. The third group of interventions is aimed at strengthening the productive and emission reduction capacities of forest enterprises, including smallholder and community small businesses and cooperatives, as well as medium and large forest firms, by leveraging private sector investments. Small forest enterprises on private and public lands (plantation owners, cooperatives, small and medium businesses, forest contractors, etc.) are often constrained by weak business capacity, limited access to finance and lack of information on the downstream value chain of the sector. Medium and large enterprises that manage larger area concessions of natural forests, planted forests, and ecosystem restoration face different challenges such as onerous licensing, land tenure and community disputes, forest certification, integration with smallholders and communities and, the downstream value chain. Innovative and transformative investments are needed for all scales of forest enterprise, particularly those initiatives that highlight their potential to reduce forest carbon emissions. Motivated forest enterprises will be selected from both forested and deforested regions of Indonesia, and where forest product demand remains high. Interventions with enterprises in communities adjacent to natural forests are intended to reduce degradation and associated emissions, while those in non forested areas will enhance carbon stocks through planted forests. Interventions will address the need to develop viable forest business models, which include:

- (i) Organizational and business capacity for business operations.
- (ii) Incorporation of sustainable forest management (SFM) principles (i.e. reliable forest inventories, sound volume projections based on sustainable cut levels, reduced impact logging (RIL), etc.).
- (iii) Adherence to MDB social and environmental safeguards.
- (iv) Facilitating reciprocal relationships with other enterprises along the forest value chain and strategic community investment by larger companies in rural communities.
- (v) Building multiple revenue sources from forests (e.g., timber and non timber products, payments from ecosystem services such as carbon and water, and agroforestry).
- (vi) Access to financial support modalities such as grants, loans, credit, off take agreements, advance payments, and guarantees. The FIP concessional financing will be particularly supportive to engage financial intermediaries such as local banks, credit agencies and lead firms. Improved access to financing will also help to leverage additional investments in small forest enterprises from public forestry support programs and private sector investors who currently view these investments as economically unviable and high risk.

The forest enterprise initiatives will support the SFM principles adopted by the Forest Management Units (FMU - KPH) being established throughout Indonesia and where possible, will support the private sector role in the longer term goal of FMU self sustainability.

III. NEXT STEPS

23. The Joint Mission has decided to submit the Investment Plan for endorsement by the FIP sub-committee at its meeting in May 2012. The tentative schedule for various tasks is given below.

Task	Responsibility	Tentative deadline
Version One Forest Investment Plan	GOI and MDBs	Late January 2012
Review of Forest Investment Plan	GOI	Early February 2012
Web-Posting of Draft Forest Investment Plan	GOI	Mid-February 2012
Peer Review of Investment Plan	GOI and MDBs	Mid-February to Mid-March 2012
Incorporation of comments and preparation of final draft of investment plan	MDBs and GOI	Mid-Late March 2012
Submission to CIF AU	GOI	Late March 2012
Review by FIP Sub-committee	Sub-Committee	April 2012
Presentation and Endorsement	FIP sub-committee	May 2012

Annexes:

Annex 1: Agenda of the Joint Mission

Annex 2: Summary of Various Meetings, including the list of people met

- Annex 2.1 Government Ministries, Agencies
- Annex 2.2 Private Sector
- Annex 2.3 Civil Society
- Annex 2.4 Development Partners
- Annex 2.5 National Workshop