

## Forest Public Benefit Function Fee in Croatia<sup>1</sup>

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### Brief summary of the case

The Forest Public Benefit Function Fee is a charge which is paid by companies and other business associations, once a year, since the fee's introduction in 1983. Initially the charge was collected by the State-owned company Hrvatske Šume at a rate of 0.07% of total income. Currently, 0.0265% of the total income charge is managed by the Ministry of Agriculture and Forestry and distributed to the beneficiaries.

According to the annual reports for 2015 and 2016 the scale of the revenues has dropped from EUR 63.88 million in 2010 to EUR 24.66 million in 2015 and a further 4.93 million reduction is expected in 2016. Besides management and restoration of forests on karst<sup>1</sup>, significant funds are spent for demining activities (10%), firefighting (5%) and scientific work (5%) (Ištok, 2016). The control of the spending is done through Committees nominated by the minister which approve the operational plans and monitor the spending, select the scientific research projects, approve and monitor demining processes and funds for firefighting.

## 1 Description of the design, scope and effectiveness of the instrument

### 1.1 Design of the instrument

Because of the great value of public benefit functions and on the basis of the direct benefits of biomass production, forests in Croatia are declared as goods of the highest interest for the Republic of Croatia in the Constitution and therefore benefit from so called close protection (Article 52. of Constitution of Republic of Croatia).

After the independence of the Republic of Croatia, the 1990 Law on Forests (official Gazette 41/90) adopted the Forest Common Benefit Function Fee originally introduced in 1983 in the Yugoslavian Forest Act (Hrvatske šume, 2013). The charge is paid by companies and other business associations which conduct economic activities on the territory of Croatia, except for companies and other legal entities who manage the forests. Initially the charge was set at 0.07% of total company income, on the special account of national forest management company "Hrvatske šume". In June 2010 the Ministry of Agriculture and Forestry decreased the charge rate to 0.0525% and a further reduction was made in February 2012 to 0.0265% of total income.

### 1.2 Drivers and barriers of the instrument

The forest public benefit function fee was introduced in order to secure dedicated funds for:

- Management and restoration of forests on karst
- Forest protection

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<sup>1</sup> Karst topography refers to landscapes formed from the dissolution of soluble rocks such as limestone, dolomite, and gypsum, and characterised by underground drainage systems with sinkholes and caves.

- Forest restoration after fires, wood withering or other disasters
- Development of forest roads
- Demining of land mines<sup>2</sup>
- Financing of programme development for private forest owners
- Preservation of genetic diversity
- Forestry research (scientific work)

Of the 2.68 million hectares (ha) of forest in Croatia, around 1.14m ha (43%) are located on karst (Istria, coast, part of Lika and Dalmatia). Forests on karstic terrain consist of very small trees which are not of interest for the timber industry, so the national company Hrvatske šume cannot generate income from management of these large areas of forest. It can be concluded that those forests have a high value of common benefit functions, but low and almost insignificant value and usability of biomass, which is crucial for the sustainable management of forests. (Ištok, 2015)

Public opinion of the Forest Public Benefit Function Fee is bad. One of the identified reasons is that the purpose of the instrument is not clear to the public, and the public is unaware of the contribution of the fee to the protection of forests (Hrvatske šume, 2015). This strong negative opinion, together with advocacy by the business association, has already resulted in two changes of legislation where the percentage of the fee was cut from 0.07% to 0.265% of total income of the companies that pay the fee. The official justification of these cuts was to decrease the tax burden of the Croatian industry.

### 1.3 Revenue collection and use

According to annual reports (Hrvatske šume, 2015; Hrvatske šume, 2016), the scale of the revenues has dropped from EUR 63.88 million in 2010 to EUR 24.66 million in 2015. The gap is explained by the reduction in the fee in 2010 and 2012. According to the annual reports, the funds are spent as follows:

Purpose	2011 (%)*	2012 (%)*	2013 (%)*	2014 (%)	2015 (%)
Forest restoration	62	69	68	71.9	80%
Private owners' forests	11	13	20	11.2	
Demining	19	10	4	11.2	10
Firefighters	5	5	5	4.5	5
Scientific work	2.4	2.5	2.5	1.2	5

\*Tikvić (2015)

Since 26 February 2015 the fee is being paid directly to the Ministry of Agriculture and Forestry; previously it was paid directly to the state owned national forest management company Hrvatske šume. This change did not affect the strict policy of targeted spending of the funds, only the fact that the state now manages the funds and pays the services to the

<sup>2</sup> In 1997, land mines were still present in 234,000 ha of forests after the war in Croatia; currently 38,000 ha still have mines

Hrvatske šume. Additionally, other beneficiaries of the funds are Advisory Service – forest department<sup>3</sup> and other public institutions who manage the forests selected for scientific work. The control of the spending is done through Committees nominated by the minister which approve the operational plans and monitor the spending, select the scientific research projects, approve and monitor demining processes and funds for firefighting. According to the Ordinance on procedures for obtaining rights for finances from the fee (Official gazette 22/2015) the members of committees are forestry experts and ministry representatives (5 members).

#### **1.4 Environmental impacts and effectiveness**

The environmental impact of this fee is significant but not measurable as in most cases the spending is related to natural disasters, extreme climate related situations, biotic situations and fires. The only measurable unit in terms of concrete figures is the area of restored forest. In 2015, 6,774.5 ha of surface were prepared for natural forest development and 28,073 ha of young forests were cared for (Hrvatske šume, 2016). Since 2014, this represented a 1,689.5 ha increase in surface area prepared for natural forest development, but a decrease of 2,797 ha of young forests being cared for; there is therefore no visible evidence that efficiency increased or decreased. In total, the overall spending on all activities decreased by 2.3% (Hrvatske šume, 2015).

Additionally, the fee is important in supporting work on forest fire prevention (32% of the total investments of the fund) (Hrvatske šume, 2015). Before the introduction of the fee, on Croatian karst, only 58 km of constructed firefighting passages existed with elements of forest roads. By the end of 2016 Croatia has constructed in total 361.66 hectares of firebreaks/firefighting passages. This includes 7,065.61 km of passages with forest road elements, 984.42 km of forest roads and 184 monitoring posts (Ištok, 2015), which have significantly increased the capacity of Croatian firefighting squads to identify and extinguish forest fires more effectively and quickly, which has probably led to many fires being prevented. In 2015 3,118 ha of state owned forests were demined and currently 35,525 ha of forests still remain under mines. After the war in Croatia, the fee financed the demining of 52,631 ha of forests. (Tikvić, 2015)

#### **1.5 Other impacts**

The cost of the instrument affects solely business entities and the final fee paid is rather low. However, the fee is considered to be one of too many parafiscal taxes for companies and it has a generally bad image. However, considering the fact that in 2015 alone, 3,149.907 m<sup>2</sup> of forests have been demined (Hrvatske šume, 2016), it can be stated that the social impacts of the fee are positive. Currently, there are still 35,525 ha of national forests that contain mines and the future incomes from the described fees are expected to help with demining in forests near Petrinja which are considered the most mine polluted areas in Croatia. In the period from 2005 to 2015, EUR 52.5 million were invested from the revenues of the Forest Public Benefit Function Fee. (Ištok, 2015)

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<sup>3</sup> Public advisory institution for services in agriculture, fishing, rural development and forestry

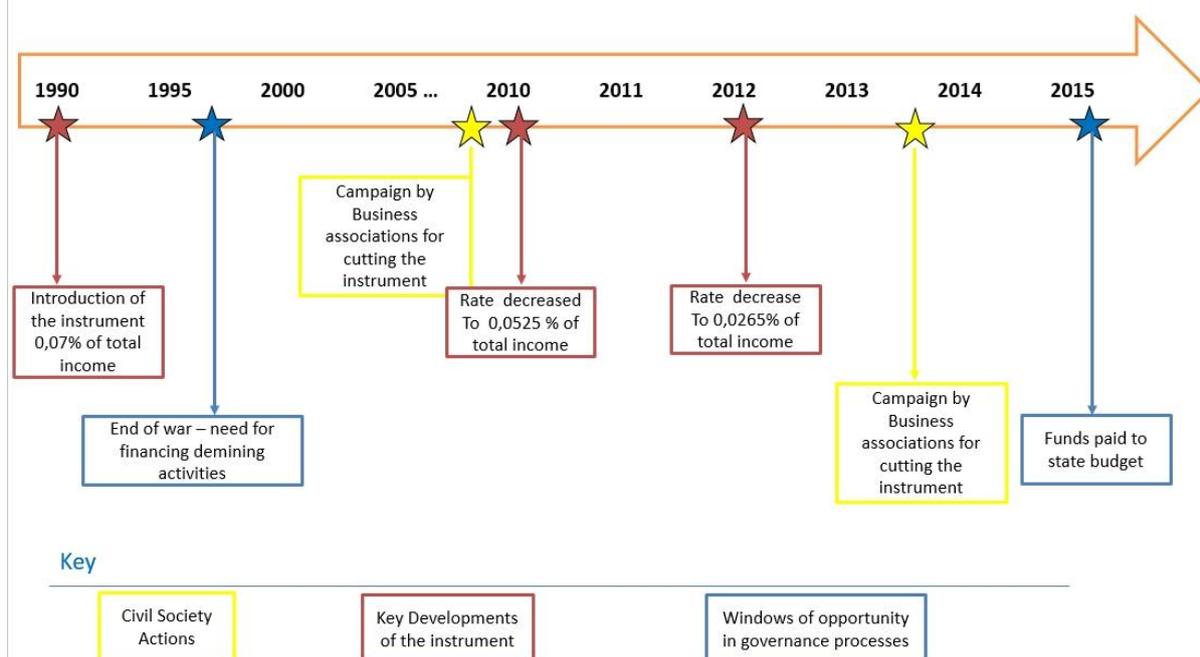
## 2 Stakeholder engagement

A decision making process was held in 1990 when the first Croatian parliament adopted the Forest Act, even before Croatian independence. Civil society and business associations did not exist at that time so stakeholder engagement was insignificant or non-existent during that period. In 2010 during the economic crisis in Croatia, the Croatian Government decreased the fee from 0.07% to 0.052% of total income of the paying companies, justifying the decrease by arguing that it helped to preserve jobs (Croatian Government, 2010). Stakeholders were also not very visible in 2010, but in 2012 when the second fee decrease occurred, industry undertook a serious campaign to cut the fee. The major stakeholders involved were the Croatian Association of Employers and the Chamber of Commerce, who succeeded in encouraging the Croatian Government to cut the fee by an additional 50% with the same justification. Since 2013 several campaigns have been launched by different business associations for the fee to be abolished, claiming that it is equivalent to a “parafiscal tax” or an “air tax” (Babić, 2015).

During 2013 the Croatian Chamber of Forestry and Wood Technology Engineers conducted an advocacy campaign to keep the fee. During that campaign, the Chamber obtained a written position statement from the Ministry of Environment and Nature Protection that the fee should stay in place, with a proposal to return to the original 0.07% level after the economy recovers. (Hrvatske šume, 2013)

In 2015 the beneficiary account for fee collection was changed from the state-owned Croatian Forests company to the Ministry of Agriculture as a result of constant accusations of advocacy groups that the funds were not being spent according to the division prescribed by national laws.

## Timeline of Key Developments in The Forest Public Benefit Function Fee



### 3 Windows of opportunity

The instrument was introduced in 1983 so there is no information available about the policy process, although it is certain that there was no public involvement (since NGOs were not allowed at the time) or consultations held.

### 4 Insights into future potential/reform

#### 4.1 Actual Planned reforms and stakeholder engagement

The only planned reform of this instrument is an additional 20% reduction in the fee (as one of many fees identified as parafiscal taxes in Croatia) according to the decision taken by the Croatian Government on 27 July 2016. This is included in a list of planned tax cuts that require changes in the law, but since there are elections in September, it remains to be seen whether this decision will be implemented. The most prominent stakeholder against this instrument is the Croatian Employers Association. Apart from the Government, no significant support by other stakeholders for keeping the current rate has been publicly identified. It should be noted again that this instrument was introduced in 1990 and attracts no publicity in the country.

## 4.2 Suggestions for future reforms – instrument design and civil society engagement

Future work on demystifying the spending of these funds and better public communication is needed, as it is obvious that this fee is under attack whenever there is public discussion about unnecessary taxes. This could also be done through the opening of the use of the funds by other associations (e.g. NGOs, schools and universities) who actively work on the issue of forest protection and management. This activity could be easily operationalised through calls for proposals for funding.

## 4.3 Suggestions for replicability

The Forest Public Benefit Function Fee can be easily replicated in all countries where financing of the forest management is a problem (e.g. Mediterranean countries). As indicated above, this fee was mainly introduced to support the management of karstic forests that do not have sufficient biomass to be sold to finance their sustainable management, including fire risk prevention.

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