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October 15, 2011

## The empire Sino-Forest built and the farmers who paid the price

By MARK MacKINNON  
 From Saturday's Globe and Mail

*How the TSX-listed company used China's historic land transfer to snare the forests now at the centre of the company's alleged fraud*

This tiny hamlet, a huddle of a few dozen mud-brick and wood homes high in the mountains that are the craggy climb to the Tibetan Plateau, is the kind of place where nothing ever happens. The pace of life is such that cattle can stand for a long while in the middle of the town's lone dirt road without disrupting traffic, which even at the busiest times of day is only the occasional lumbering truck.

So when a quartet of officials from the county forestry bureau arrived one day three years ago, driving all over the mountains with odd-looking machines in their hands, it caused quite a commotion. Even still, none of the nosy residents could have anticipated that the arrival of the four men with the hand-held GPS devices was a moment that would bring that rarest of commodities to Anjia: change.

The arrival of the forestry officials dumped the unprepared residents of Anjia, a corner of China's Yunnan province that seems to exist in the 19th century, and dozens of others like it, into the world of 21st century finance. An effort to reform China's forestry industry - which was supposed to help close the wide wealth chasm between the country's rural and urban halves - resulted instead in a parade of swindlers and middlemen to places like Anjia, persuading the locals to

sign away the usage rights to their land for a pittance, then selling it to bigger foreign and domestic companies that were looking to cash in on one of the biggest property transfers in history.

In the case of Anjia and three other towns around it, the end buyer was Sino-Forest Corp. TRE-T, a Toronto-listed company run by a Hong Kong entrepreneur, Allen Chan, who devised a way to profit from that land shift and from Canadian investors' hunger for a Chinese growth story. By accumulating tracts of forestland all over China - then raising billions of dollars from investors to do it over and over again - Sino-Forest grew to be the largest forestry firm on the Toronto Stock Exchange, at one point valued at some \$6-billion, until it came crashing down this summer under allegations of massive fraud. In late August, Mr. Chan quit as chief executive officer and four other executives were put on leave or stripped of their duties while the company and the Ontario Securities Commission investigate.

Among the key allegations is that Sino-Forest exaggerated its timber holdings: It claims to manage nearly 900,000 hectares worth about \$3.5-billion, mostly in southern and eastern China. Whether or not the company really controls so much forestland, and whether it is as valuable as it says, is the central question of the Sino-Forest saga, the answer to which may not be known for months.

But what is already clear is that the residents of remote villages like this one - the obscure places where Mr. Chan and others like him built empires based on land and trees - saw only a tiny fraction of that money, just enough to cause a brief spark of prosperity that disappeared as quickly as it came. In Anjia, life has already returned to the normal it knew before the national forestry reforms began.

At first, it all seemed like change for the good. The men with the GPS devices came down from the mountains with startling news: Under a new policy drafted in Beijing, the forestland around Anjia now belonged to the hamlet's 420 residents. Six decades after the Communist Revolution outlawed private landholding, the bewildered villagers were handed little green booklets outlining how much of the surrounding mountains each of them now owned. Many shrugged, unsure of what it really meant given that they considered the thin forests of Yunnan pine to be almost useless. "The trees are no good," said Yang Wusa, a corn and potato farmer in the nearby hamlet of Nongchang. "We cannot even use them to build pig sties."

That didn't seem to matter. A short time after the forestry officials handed out the little green books, Anjia started seeing more visitors: Next, a trio of slickly dressed men from the nearby city of Ninglang showed up, spinning tales about how those little green books could be sold for cold, hard cash. The village secretary, An Zhashi, was intrigued, particularly by a promised side agreement that would see him paid 50,000 yuan (about \$7,500 Canadian, using the average exchange for the past 12 months) to get the whole village on board.

The deal on offer seemed a simple trade: The brokers would lease all 6,701 mu that had been allocated to the village, in exchange for a one-time payment of 130 yuan per mu. A mu is a Chinese unit of land measurement; 15 mu make up one hectare. So the Anjia agreement involved some 447 hectares for a total payment of about \$130,000, or about \$292 per hectare.

It would be a 50-year lease, and there was no description - or restrictions - in the one-page contract regarding precisely what the brokers, or anyone they sold the lease to, intended to do with the land or its trees.

"The brokers came to us and they persuaded us by saying, 'The trees are so far

from the village, there's no road up, and that this (privatization of forestland) is a new national policy that we should co-operate with,' " Mr. An recalled in an interview at his family home, which has just undergone a renovation that he says was paid for by his share of the proceeds from the forestry transfer. "They persuaded us to sell."

He grimaces when asked if he and the villagers got a good deal. "We didn't know that in the future the land would be worth 180 yuan or even 290 yuan (per mu). We sold it too cheap."

If Mr. An had phoned around to other villages like his in remote corners of China, he might have received some useful warnings. In the thickly forested south of Yunnan province, near China's border with Myanmar, villagers are still smarting over a series of trades in 2005 that left them with just 30 yuan per mu (about \$67 per hectare) and saw vast tracts of remote forests transferred eventually into the hands of Sino-Forest, only to see them wildly increase in value.

And in coastal Guangdong province, the head of another village that sold to Sino-Forest says he's hoping the company's troubles will result in the forestland being transferred back to the farmers, so they can try to sell it again - and perhaps get a fairer deal the next time around.

### A grand plan for forestry

For more than two decades after Deng Xiaoping introduced the principle of "household responsibility" to the country's farmlands, China's forestry industry remained trapped in time. According to the country's post-revolutionary constitution, the forests were owned by rural collectives. In practice, that meant the government, and for decades it was local bureaucrats who managed - and often mismanaged to the point of exhaustion - the country's 175 million hectares of forests.

In 2002, Beijing introduced its first major forestry reform, the Rural Land Contracting Law, which transferred the forestry usage rights to individual households for terms of 30 to 70 years. Five years later, another law entrenched that privatization by allowing the usage rights to be extended in perpetuity.

Like nearly all major decisions in China, the decisions were announced by the powerful Central Committee of the Communist Party. "Develop the forestry sector, and bring prosperity to the economies of mountainous regions," was the instruction that went out in a September 2008 Central Committee missive that would be interpreted down the governing pyramid as encouragement to accelerate the pace of China's great tree sale.

As usual, the government would later give itself top grades for the effort, despite statistics that showed the urban-rural wealth gap continued to expand rather than shrink. This March, Premier Wen Jiabao - during one of his annual (and heavily scripted) question-and-answer sessions with Chinese Internet users - faced multiple questions about the widening income gap between the increasingly rich urban China and the still desperately poor countryside. He pointed to the forestry reforms as a success story in shrinking that divide.

"We believed we could significantly change our forestry production if we reformed the ownership of these collectively owned woodlands like we contracted out the use of arable land to individual households, so that farmers could operate those woodlands like operating a business," Mr. Wen wrote in reply. He went on to say that he had recently visited a mountain village and concluded that "the reform has indeed changed their life."

Which village Mr. Wen visited was left unnamed in the official transcript, but it couldn't have been Anjia or any of the half a dozen other villages visited by The Globe and Mail in Yunnan, Hunan and Guangdong provinces during a lengthy investigation of Sino-Forest's businesses in China.

What happened in Anjia appears to be far more representative of how the reforms have gone. Instead of a massive wealth transfer from urban China (and foreign corporations) to the impoverished countryside, the Rural Land Contracting Law and its successor documents resulted in a massive property transfer that saw many villages tricked or coerced into selling the green booklets that were supposed to transform their lives. Many of those on the losing ends are members of some of the China's 55 ethnic minority groups, populations that have been almost completely left out of the country's remarkable progress over the past two decades.

Li Ping, a lawyer working in the Beijing office of Landesa, a Seattle-based organization that promotes rural development, said there was little question in his mind that Sino-Forest and other big foreign and Chinese companies had abused the spirit of the forest reforms. "They definitely took advantage of the farmers. Chinese law requires it to be an informed transfer - not taking advantage of the farmers' (ignorance) of the market price of their land." Sino-Forest, for its part, says it deals only with the middle companies, thereby distancing itself from how local landowners were treated in the deals.

In several villages The Globe and Mail visited in Yunnan, none of the farmers who remained the theoretical landlords of their forests had any documentation regarding precisely what rights they had given up and retained when they agreed to the long-term leases. "There were too many middlemen involved. The middlemen have bosses, and those bosses have bosses. In the end we don't even know who we sold our land to," said Yang Wulin, head of Madiangou, a cluster of homes on the eastern edge of the regional centre of Ninglang that is populated with farmers who moved to the fringes of the city after selling the forestlands their families had long lived on.

Despite their decision to move, Mr. Yang said the 190 residents of Madiangou had together received only a 20,000 yuan "deposit" in exchange for their collective 1,000 mu. It was unclear how they expected to collect on the rest of the 180,000 yuan (\$27,000) they had been promised. "We have no contract, no telephone number, no name," said Mr. Yang, who said he - like nearly all of the villagers - is illiterate and couldn't read the deal he had signed. "We just gave our (land certificates) to the middleman."

A middleman makes good

One of the brokers involved in the land swaps that would see the forestland around Anjia transferred into the hands of Sino-Forest was Shen Ji, a small-time Ninglang trader in his 30s who had lived an unlucky life until he heard about the coming forestry reforms. By his own description, he and his five sisters grew up poor, and he left school after third grade because his parents needed his help tending their plot of potatoes, corn and buckwheat. Like many of the farmers he would later buy the forest leases from, he can't write anything but his own name. But he says he can "almost" read.

Mr. Shen said he began travelling to the villages around Ninglang and buying up the land certificates before such trades were even legal. At the beginning, he says, he could get the farmers to agree to sell their land for as little as 20 or 30 yuan per mu (\$45-67 per hectare). Later, he says, the price rose as word spread among the villages about how much the land might be worth. Sometimes, he

convinced the villagers to give him the land deeds in exchange for only a promise to pay them back when he sold the forests onwards.

By early 2010, when he heard that a representative from a major foreign forestry company was in town looking to buy forestland, Mr. Shen was the broker in town with the largest collection of deeds to local forestland, roughly 160,000 mu or more than 10,000 hectares. Dressed in the best clothes he could afford, he went to the Ninglang hotel where a representative of "Jia Han" (as Sino-Forest is known in China) named Mr. Shi was known to be staying.

"At first they refused to see me, because I was wearing cheap clothes and they didn't trust me," Mr. Shen recalled. "So I went to their hotel room holding all my ownership certificates." They let him in, and eventually he sold 24,000 mu of forestland to Sino-Forest, including, he says, the land around Anjia.

Mr. Shen says Sino-Forest seemed oddly uninterested in buying the better forests he had acquired - "their standards were very low" - and instead focused on cheaper properties like those around Anjia. He didn't care, as long as he could convert some of the paper deeds he had accumulated into cash.

There was a hitch: Sino-Forest, as a Hong Kong company listed on the Toronto Stock Exchange, needed a local partner in order to buy Mr. Shen's forests. A new company, Yunnan Shunxuan, was born and the sale went through.

Mr. Shen said it was clear to him that Yunnan Shunxuan - which is portrayed in company documents as an unrelated party that later sold the forest rights on to Sino-Forest - was always just Sino-Forest under a different name. "Shunxuan is part of the Sino-Forest brand. The people from Shunxuan were the same as the people from Sino-Forest," he said. "No matter if it was Sino-Forest or Shunxuan, it was always Mr. Shi that I met with."

(One of the key allegations - still unproven - against Sino-Forest is that it inflated the value of its properties through sales between related parties. When The Globe and Mail tried to visit the street address in the city of Kunming given in Sino-Forest documents as the headquarters of Yunnan Shunxuan, the given address didn't exist. When questioned, Sino-Forest produced a second set of coordinates for Yunnan Shunxuan that turned out to be a hotel room with no sign on the door. The woman inside refused to answer questions.)

Mr. Shen offers no sympathy to the farmers whose land he bought as cheaply as he could and sold onwards at what he says was a modest profit. The forestry reforms may not have transformed rural China as they were supposed to, but they have made a richer man out of Mr. Shen. The school dropout now drives around Ninglang in a black Mitsubishi SUV, a mobile phone constantly on his ear.

"My life has improved a lot. Because of the money I've made, all my five sisters have been able to move into the city," he says. But the good times, he fears, are almost over. "There are so many people in this business now. They've heard there's money to be made."

A village (temporarily) prospers

When Anjia's 83 heads of household were called together on Sept. 23, 2010, Mr. An, the local forestry officials and the trio of brokers portrayed the offer on the table as money from the sky. The villagers would be paid 130 yuan per mu for the rights to land they never used anyway. The revenue from the sale would be shared equally, meaning most households could expect to receive some 10,000 yuan (\$1,500) in exchange for a 50-year lease on the forested mountains that

surround Anjia like a giant green city wall.

That the vote passed 83-0 was no surprise. Decisions made by authorities are rarely challenged in this part of China, and because the land was owned by the individual households (even though they were bargaining as a collective), the deal Mr. An signed with the brokers included a 100,000 yuan penalty should any household opt out and thereby mar the contiguity of the parcel being sold. Everyone in town knew this, and any vote against the deal would be sure to incur the anger of the rest of the villagers, who all belong to the country's Yi minority.

The deal likely would have got wide approval without such coercion. Before the brokers came to offer them money for their land certificates, Anjia scraped by on subsistence farming only. Skyscrapers here are the sunflowers and corn stalks that stretch above the low-rise crops of tobacco and barley.

As China has raced ahead to become the world's second-largest economy in recent years, places like Anjia have been left further and further behind. Sparks of modernity - such as electricity poles and tiny satellite dishes that allow residents to watch domestic state-run television - only highlight how far behind the times these hinterlands lag. None of the homes in town has a toilet, and the lone, unlit dirt road is so narrow that if a truck comes along, smaller vehicles have to back up, sometimes all the way back to the village.

The money finally arrived in March, after the land was sold by Mr. Shen to Sino-Forest. Villagers were told they needed to travel to Ninglang and open bank accounts so that they could withdraw the cash. Like most in town, 38-year-old Luo Rida couldn't believe his good fortune. Within days of withdrawing the cash, the father of three had purchased a new television set and a Chinese-made Zongshen motorbike that he says will allow him to save money driving back and forth to Ninglang. "I spent it all," he said, kicking at stones on the ground outside his mud-brick home.

His 35-year-old brother, who lives on the neighbouring plot, came closer to spending his share of the money the way bureaucrats in Beijing had hoped, using it to pay for another year of secondary school tuitions, boarding and books for his two teenage daughters.

"We hope their knowledge can change our lives," Luo Ase said, speaking of his absent daughters, as his 10-year-old son played on a pile of firewood. "If the money had not come in, we could not have afforded for them to go to school this year. Next year, they will have to come back home and find work."

### Feelings of regret

If the residents of Anjia had sought it, they might have received some valuable advice from other farmers in other parts of China who also sold their land rights, only to later feel as though they'd been taken advantage of.

The rain forests in the south of Yunnan are lush and more productive (though logging in much of the region is prohibited by Beijing) than those in the colder northwest of the province, so the brokers got there first, buying up the local farmers' land rights years before they turned their attention to places like Anjia. In Mang Mei, a tiny clutch of red brick homes that cling to the sides of a swerving mountain road in the far south of Yunnan, the villagers were convinced by a broker to agree to lease away their 6,200 mu of forestland for 30 years in exchange for a one-time payment of 200,000 yuan (\$30,000) or about 32 yuan per mu. As in Anjia, the broker sold the land on to a middle company, which

eventually found an end buyer in Sino-Forest.

Na Gelie, the 44-year-old grandmother who is the deputy head of Mang Mei's village council, said the town was initially bewildered at why anyone wanted to pay them for the rights to forests around them, particularly since the predominantly birch forests had been cut just before the reforms took effect, meaning it would be years until there would be any new trees to cut.

Later, as the value of the forestland around them soared, the 3,694 residents of Mang Mei understood they had been snookered. They charged Ms. Na with trying to get someone - the broker, the middle company, Sino-Forest - to renegotiate a better deal. "The price that the ordinary people got for their land is very cheap. They didn't get a fair deal," Ms. Na said. "Last year, I and (the village leader) went to go visit the broker to ask if we can get more compensation from Sino-Forest, but we got no response from the company. We will try again this year."

Certainly, there's no evidence here that the local residents were sitting on top of property that was valued by international investors. Livestock roam the unpaved roads, and half-naked children play in the streets as the sun sets. After dark, electricity is scarce. And the money that was supposed to change residents' lives is long gone. "Some households might have saved some of it in the bank, but the families I've talked to all spent it," Ms. Na said.

Ms. Na said two villagers had been hired to act as "forest supervisors" - putting out fires and keeping an eye out for illegal logging - but otherwise the town was no longer getting any economic benefit from the forests around them.

Similar stories are told in coastal Guangdong province, the region where Sino-Forest first launched its strategy of buying and selling swaths of "standing trees" (as in, buying and selling forestland without cutting or replanting on the properties), and where it still keeps its China headquarters.

In Tangkong village, a 90-minute drive from China's southeastern business hub of Guangzhou, the local Sino-Forest affiliate, known as Jiayao, bought the rights to 800 mu of forest directly from the village council. They signed a 70-year deal in 1996 that would see the farmers collect 40 per cent of the revenues from their land. Then the company returned in 2009 and renegotiated a new, shorter lease for 50 yuan per mu per year - about \$110 per hectare - that otherwise cut the farmers out of the profits.

Wu Yunwen, deputy head of the Tangkong village committee, said some of the villagers wanted to hold out for a better price in 2009, "but after some hard work by the local government, we persuaded them" to accept the new contract. The local government, he said, used the proceeds from the sale to pay for village improvements, and then gave each resident a share of what was left over.

Mr. Wu said it was clear to him that Sino-Forest had high-level *guanxi*, or connections, in the local government. "Otherwise they would not be so well taken care of." No other buyers ever approached Tangkong about buying their forest rights. "If we had the chance to rent our land to another company, maybe we could have gotten several hundred (yuan per mu). But we had no other choice."

Like most people contacted for this article, Mr. Wu said he had not heard of the allegations against Sino-Forest, or the precipitous drop in the company's stock price. When told about the company's troubles, the village head shrugged. "If they stop paying us on time, maybe we can go and get a better deal on the market."

'It's very strange'

Back in Anjia, residents feel the same about the surrounding forests as they did before the reforms began in 2002. They provide nice scenery, they're a place to collect firewood, but they're someone else's property. Before, the trees belonged to the government. Now, they belong to Sino-Forest.

The whole episode left Luo Rida and his family up one motorcycle and one television set. His brother Luo Ase's daughters will have an extra year of schooling. Standing among the chickens and flies that rule the courtyards of both brothers' homes, it's clear that while the influx of cash was welcome, it did little to close the gap between 19th century Anjia and the 21st century China of Guangzhou, Beijing and Shanghai.

Anger over how the forestry reforms have been carried out is scattered, but widespread. The complaints have reached the ears of forestry bureau officials in Yunnan province, who, after initially facilitating the speedy land transfers, are now slamming on the brakes.

"We've suspended all transfers of land because we are changing the policy," Xiong Zaiping, deputy director of the Ninglang Forestry Reforms Office, said in an interview. The new rules, he said, would mandate that government experts determine the value of all forestland before any new leases are signed, and the overall value of the contract will have to be within 10 per cent of that official evaluation. A minimum price of 180 yuan per mu (about \$400 per hectare) will also be introduced to make sure villagers get fair payment for their lands. "In the past, the benefits of the reforms were not fully enjoyed by the farmers. The companies made too much money," Mr. Xiong explained.

While the new rules appear to have been introduced in April - before the allegations against Sino-Forest - the company's troubles are definitely on the radar of officials here. In the provincial capital of Kunming, officials in the Yunnan Forestry Bureau said they're investigating not only how much land Sino-Forest actually owns in the province but the process under which the lands were acquired. An official told The Globe and Mail in June that the company's statements don't match their own.

Aqi Duzhima, the head of Wenquan village (the municipality that Anjia belongs to), said the forestry reforms enriched the wrong people and left her region no better off than before the land transfers began. "We didn't know what our land was worth," Ms. Aqi said, adding that three of the five hamlets of Wenquan that agreed to sell their land have yet to receive a single yuan from the buyers who took their land certificates.

"It was a case of 'give us that piece of paper (the land certificates), and I'll give you some money for it.' It was easy money. To be honest, the people here are poor, they are only worried about what they can see in front of them. They have no eye on the future, on how their children will live."

But Ms. Aqi isn't sure that her village lost the trade. She said one of the most mysterious aspects of how Sino-Forest and other companies bought up all the forest rights in this corner of Yunnan is that she and others don't believe the trees are worth very much.

"We feel like they just wanted our (ownership) certificates. They don't cut the trees, they never came back to the mountains. We feel like the land is useless, but they wanted it anyway. It's very strange."



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