



**COUNCIL OF
THE EUROPEAN UNION**

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LIMITE

MEETING DOCUMENT

from : General Secretariat of the Council

to : Working Party on Forestry

Subject : Proposal for a Regulation of the European Parliament and of the Council laying down the obligations of operators who place timber and timber products on the market

With a view to the meeting on 3 December 2008, delegations will find attached a note from the Commission.

GENERAL

- **Proportionality**

Illegal logging is an important cause of biodiversity loss and a significant contribution to deforestation, which in turn is responsible for 20% of global greenhouse gasses. Apart from undermining good governance, sustainable development and the rule of law in countries it is present, illegal logging also undercuts at global scale the competitiveness of legitimate forest industry operations through price dumping due to the affluent supply of cheap, illegal timber and the degeneration of the image of timber as a sustainable and ecological material. The industries in the EU that produce and trade in legal timber and timber products are put at a disadvantage as they face unfair competition from cheap illegal timber. The proposed measures approach the issue as a matter of joint responsibility between producers and consumers. Not only do we need to address the illegal cutting of timber but we also need to address the purchase of that timber. It is true that most illegal logging occurs outside the EU although evidence suggests that it is also an issue in some EU Member States. Tackling only the import of timber and timber products would both be ineffective and discriminatory. It would also be inconsistent with the international trade rules in the absence of equivalent conditions for domestically produced timber. The proposed measures are the least trade-restrictive and cost-intensive. Inside the EU governments and the timber sector has established forest management and purchasing procedures which should be sufficient to ensure legality. It is therefore not expected that the proposed measures will be create additional burdens, as the requirement to respect existing laws and regulations exists already and should be strictly enforced.

- **Administrative burden and costs**

Estimates for the overall administrative costs of the various options were made as part of the impact assessment. The costs for the non-EU timber industry resulting from the implementation of the proposed Regulation are estimated at approximately € 29 million per year.. Costs for the EU private sector are likely to amount to approximately € 40 million annually.

Many high-volume producers and importers, such as the pulp and paper industry or timber traders organised in trade federations already have checking/tracking systems and/or due diligence requirements and systems in place and are already carrying out the checks and supply chain controls that the proposed Regulation aims to make mandatory. This means many European operators will not have to incur significant additional costs for putting in place new systems. The same applies to many third countries. For developing countries the option of engaging in FLEGT VPAs. There will also be, funding available to assist FLEGT partner countries in meeting the costs of providing legality guarantees, where this is necessary.

The costs to operators under the proposed Regulation are also relatively light when compared to the options originally assessed. The option of mandatory proof of legality by EU traders (option 4B) was estimated to lead to an annual cost of € 136 million. The regulatory costs will be also considerable lower compared with the "control activities" by government authorities under option 4B. As the focus of compliance and enforcement is directed at the verification of whether effective due diligence systems have been put in place and/or are being used by operators. The regulatory costs in the EU are therefore estimated at a mere 1 MEuro/year.

- **Legal basis and choice of legal instrument**

The legal basis of a legislative act is determined by its content and objective. Article 175(1) TEC enables the Community to adopt measures to achieve the objectives identified in Article 174 TEC. The preservation, protection and improvement of the quality of the environment is among them. Illegal logging is a pervasive problem which poses significant threat to forests as it contributes to the process of deforestation, which is responsible for about 20% of CO2 emissions, threatens biodiversity and undermines sustainable forest management. The proposed legislation puts forward measures to address the problem of illegal logging aiming at deterring the marketing of illegally harvested timber in the EU. The proposal doesn't include a trade ban or any requirements as regards the importation into the Community or the placing on the Community market of timber and timber products. The focus of the proposal is on the behaviour of the operators and not on the product. Given the absence of any trade restrictions as regards both the internal and the external trade, neither Article 95 TEC (Internal Market) nor Article 133 (External Trade) could be justified.

The choice of regulation offers the advantages of having general and uniform application, being binding in its entirety and directly applicable in all Member States, without the additional administrative burden of a national act being necessary for transposition.

- **WTO compatibility**

The proposed measures do not introduce importing or marketing requirements for timber and timber products hence they are not de jure trade restrictive. The focus is on the business behaviour that currently is not motivated to show prudence, judgement and positive action in ascertaining legality. In addition domestically produced timber is included in the product scope so as not to afford unfair protection to domestic production. The operational objective of the proposed measures is to minimise the risk of illegally harvested timber and timber products entering the Community market. It falls on the operators to implement appropriate measures based on risk management to meet that objective.

- **Strategy with EP and timeframe of adoption**

The adoption of the proposal by the legislators is somewhat complicated in terms of timing by the European Parliament elections next June. Our wish is that at least the first reading by the EP and the Councils' common position will be concluded before the EP dissolves in April '08.

- **Nationality of operator and selling technique as determining factors when assuming responsibility to exercise due diligence**

The territorial field of application of Community law is constituted by the territory and jurisdiction of EU Member States. Community law applies to intra-Community situations only hence may establish obligations insofar as the operator is located in or operates within Community territory. Community law regulating economic activities applies to all those economic activities performed by economic operators that carry out business activity within the Community even if managed or owned from outside the Community. In other words non-EU nationals, be it natural persons or companies, situated and operating professionally within the Community are subject to legal requirements under Community law as regards their business activity whenever they place timber and timber products on the EC market.

The proposed measures therefore apply to all operators that supply the EU market with timber or timber products on a professional and commercial basis. Purely personal or household activities are however excluded from the application.

IMPLEMENTING MEASURES

- **Excessive use of Comitology**

The European legislator normally concentrates on setting the fundamental principles governing the subject in question, leaving the technical rules to the experts who have the expertise and the flexibility to address dynamic circumstances quickly and effectively. The legislator is not in a position to foresee all ramifications of the rules it enacts, the application of Community legislation therefore normally relies on the delegation of powers to the European Commission to adopt implementing measures. This facilitates more efficient legislation. That doesn't mean however that the Commission has discretion in executing its implementing powers. The Commissions' use of its powers is supervised through the Committees established to advise the Commission, which comprise Member State representatives and are subject to the legislators' scrutiny. In addition, the principles set out by the legislator in the basic act set the framework and the implementing measures must respect this framework. A recent example was the work on adopting the implementing regulation to the 2005 FLEGT Regulation, which was developed with the intensive involvement of the FLEGT Committee.

The legislators' and the committees' control authority varies depending on the Comitology procedure. The strictest rules are established in the context of the Regulatory Procedure with Scrutiny (see below for details) where the Commission can adopt implementing provisions only if all parties involved (Committee, Council and Parliament) agree.

- **Regulatory Procedure With Scrutiny (RPS)**

The implementing measures foreseen in the proposed Regulation are proposed to be adopted using the Regulatory Procedure with Scrutiny (RPS). This Comitology procedure is relatively new and it applies to measures of general scope with a 'quasi legislative' impact. Amendments of the certain elements of the basic act (e.g. changes to the annexes) and any provisions that supplement the basic rules qualify as 'quasi legislative' measures and are therefore subject to the RPS.

This procedure aims at reinforcing the role of the Parliament and the Council in the process and goes beyond the traditional right of scrutiny that exists in the other Comitology processes (management and simple regulatory).

This process therefore allow the European Parliament or the Council, by qualified majority, to oppose the adoption of implementing measures by the Commission, if the Commission exceeded the implementing powers provided for in the basic instrument or if the implementing measures are found not to be compatible with the aim or the content of the basic instrument or not to respective of the principles of subsidiarity or proportionality.

- **Use existing FLEGT Committee**

A FLEGT Committee was established by Council Regulation 2173/2005 and has already started its work. Instead of creating a new Committee for the new legislation it is proposed to use the existing Committee, which has already made its first experiences.. The delegation clause (Article 11) should empower the FLEGT Committee.

- **Application dependant on the adoption of implementing measures**

The principles set out in the proposal can not be implemented or enforced before all rules are in place. It is thus necessary to tie the application of the obligations to the entry into force of the implementing rules and bearing in mind the complexities of the issues at stake that sufficient time is allowed for the adoption of these rules

- **Exclusion of energy-use timber products on the basis of the future directive**

The proposal excludes wood subject to mandatory sustainability criteria. Such criteria are foreseen in the Commission's proposal for a Directive on the promotion of the use of energy from renewable sources. Energy produced using wood biomass would only count towards a country's renewable energy target if produced in accordance with such criteria.

The Commission considered that a double burden of compliance with both the current proposal and the Renewable Energy Directive should be avoided for such wood products. Definition 2a) refers to timber and timber products subject to sustainability criteria and not timber and timber product categories. Therefore such timber and timber products whose use will not count towards the renewable energy targets would in principle be covered by the current proposal.

The proposal intends to facilitate and provide incentives for the use of legal timber and products derived there from. It also aims at avoiding duplications and unnecessary burden. In the context of the discussion of XX directive the Commission intended to facilitate and encourage the use of sustainable biomass.

Operators dealing with timber products covered by the mandatory sustainability requirements of the new directive, should therefore not be burdened by the due diligence requirements.

- **How does this proposal deal with potential circumvention under the FLEGT VPA scheme?**

The proposal foresees that the operator is deemed to have fulfilled his obligation with regard to timber and timber products that are FLEGT licensed, by the simple fact to have obtained these licenses. As regards imported products the FLEGT Regulation stipulates that FLEGT VPA countries only have to certify that these products have been legally imported. The Council at that time deemed it to be excessive to require FLEGT VPA countries to judge on the legality of the logging and production processes in 3rd Countries. As a result of this decision there may be possibility of circumvention. The Commission is trying to address this issue in the FLEGT VPA negotiations.

- **Do we intend to facilitate the adaptation of small businesses to these new legal requirements?**

Given that small businesses make up a large proportion of the forest sector an exemption for such businesses would severely limit the effectiveness of the proposed Regulation. The proposal allows such businesses to adhere to schemes of "monitoring organisations" and thus reduce set-up costs for due diligence systems.

- **Why don't we prohibit the placing on the market of illegally harvested timber as the US did?**

The impact assessment carried out in preparation of the current proposal concluded that this option was neither effective nor feasible as the following problems would arise:

- 1) Enforcement of third country's' laws: The enforcement authorities in Member States would need to establish an offence on the basis of foreign laws through investigations beyond their jurisdiction and national courts would be compelled to rule on the legality of timber products harvested in a third country based on the laws of that country. Unlike the USA Europe is generally reluctant to act beyond its jurisdiction or to pass judgement on other countries' legal frameworks unless there is an immediate threat to the well-being of its population, such as in the case of terrorism, weapons of mass destruction or on a less grandiose scale food safety or public or animal health.

- 2) Proving illegality: Obtaining the necessary proof that a specific batch of timber was harvested at a certain time and place in contravention of applicable legislation in the country of harvest is deemed to be a difficult if not, in many cases, impossible task. Practical difficulties and political implications would limit its application to very few high profile cases, thereby undermining its effectiveness in meeting its objectives. It also won't help addressing the cases where a specific countries governance framework is weak and enforcement of national laws is patchy. Such countries will be reluctant to cooperate with the EU on enforcement. Conversely such a rule could also lead to having to lend assistance to other countries, where such assistance may be problematic, due to the possibly less than perfect credentials of a third country. Not all forest producer countries have spotless democratic credentials.
- 3) Legal certainty: In the absence of concrete requirements as regards non engagement in the prohibited act judges would have wide discretion as regards interpretation. Operators would thus never be sure whether they actually comply or not.
- 4) Proportionality and objective: The overall objective of this initiative was to reinforce the international fight against illegal logging and associated trade and complement existing Community policies. Illegal logging mainly happens outside the EU. However any measures should also tackle domestic production to avoid trade disputes and reciprocal measures. The EU is a big timber consumer and as stated in the FLEGT Action Plan should assume all responsibilities stemming from its role in the international timber trade. Having said that, such responsibility should take account of the complexity of illegal logging and also of the structure of international timber trade and should not go beyond what is necessary to achieve the objective. Rather than punishing operators for illegal activities falling beyond their control it was considered more appropriate to reduce the incentives for 'accepting' an illegal activity.

DEFINITIONS

- Applicable legislation: definition seems narrower and non-compatible with the FLEGT definition

"Illegal logging" can be defined as occurring when timber is harvested, transported, bought or sold in violation of national and/ or international laws. There is however, no internationally agreed definition. What is "illegal" depends on national laws. In order to avoid any discriminatory or unfair definition existing legislation in the country of harvest should be the basis for any such definition. For the sake of legal certainty the scope of legislation to be taken into account is determined to include environmental, economic and social legislation applicable to forest management & conservation, timber harvesting and relevant trade legislation regulating forest management & conservation and timber harvesting. The scope takes a minimalistic approach compared to the approach adopted for in the negotiation of FLEGT VPAs but does not deviate from the latter.

- Placing on the market: critical point of control (first time) and implications for the definition of "operator"

Placing on the market is defined as the professional supply of the Community market with timber or timber products. This definition applies irrespective of the selling technique used and irrespective of whether the products are made available in return for payment or free of charge. Clearly personal or household activities are excluded. Imported products assume the Community status after their import into the customs territory of the Community hence importers are subject to the requirements. The requirements are limited only to the first time timber or timber products are placed on the market which means that it doesn't apply to all operators involved further down the distribution chain. In practical terms only importers for imported products and primary producers or operators who have the legal right to sell the output of the primary production for domestically produced timber are subject to the due diligence requirement. Respecting the principles of better regulation and simplification of legislation the Commission deemed it excessive to require distributors and manufacturers to demand proof of the exercise of "due diligence" from the preceding market operators. The exercise of due diligence at the first step was appeared to be sufficient to ensure an effective operation of the regulation.

DUE DILIGENCE SYSTEM

- How will the system look in practice?

This proposal sets out the procedures and measures that the due diligence system should encompass but does not prescribe in detail how these procedures and measures should be performed hence allowing the necessary flexibility for the effective functioning of the market. Implementing measures will complement the general provisions while ensuring respect for the principle of flexibility.

- How will the risk management work in practise? What could constitute a risk? Who will determine the risk criteria? Will the operator undertake both the risk assessment and the risk treatment?

Risk management is not a static process but a dynamic process in which information is continuously updated, analysed, acted upon and reviewed. In managing the risk a balance must be struck between costs and benefits as clearly it will not be cost effective to address all risks equally. Criteria will have to be established before the application of the regulation to determine what constitutes an acceptable or unacceptable level of risk. These criteria will be determined in the implementing measures. Such criteria could be product-related i.e. species, product, sector and value, trade flow-related i.e. frequency and diversion, supplier-related i.e. financial position, reputation & trustworthiness or on the basis of proven risk of which there is a record and the facts surrounding the case.

The risk determination will be done through the regulatory procedure. The risk management falls on the operators. The assessment and treatment of identified risks on the basis of the risk factors fall on the operators. Risk assessment could be done by operators themselves – most likely by larger operators, or operators with a vertically structured and short supply chain. For smaller operators it will be possible to rely on the systems and requirements established either by the “ monitoring organisations “ or by commercial operators, offering such services against a fee.

- What is meant by 'auditing' in terms of process and subject matter?

Auditing forms an integral part of the due diligence system as of any effective business management system. It's not required that it is performed by a third party. The details of this element i.e. methodology and organisational requirements will be laid down in implementing measures. In terms of scope it should cover all elements of the due diligence system, any non-compliances and corrective measures.

- What is actually required under the first element 'access to information regarding' ?

This proposal adopts the system approach rather than the document approach also for the legality component. Operators are not required to follow a specific legality verification scheme or to acquire documentary proof of legality.

ENFORCEMENT

- Who checks the compliance of the operators that make use of a recognised system? Duplication appears as both the respective monitoring organisation and the competent authorities assume that responsibility?

Enforcement rests with Member States and is a public matter hence private entities i.e. associations do not have the legal authority to sanction non-compliance for the purposes of enforcement. It is an integral part of the criteria for the recognition of a monitoring organisation that they have a monitoring system in place, which allows them to determine whether operators actually use the system they provide. The disciplinary measures they also have to put in place will however be restricted in practice to remove the certification of an operator. This monitoring function aims at ensuring orderly and effective implementation which in turn demonstrates smooth functioning of the recognised due diligence system. This is quite distinct from the power of sanction which an EU MS will have under the regulation. The removal of certification, may also lead to sanctions. There is more of a complementarity than duplication as both sides have quite different functions.

- Absence of threshold/ceiling as regards penalties could result in big discrepancies which consequently lead into a 'shopping' attitude.

With respect to the principle of subsidiarity and in view of the differences between the legal orders of Member States as regards penalties, this proposal empowers Member States to impose penalties for non-compliance with the legal requirements introduced therein. The proposal also avoids defining the specific offences for which penalties could be imposed although obviously these concern the use of a due diligence system.

- Hierarchy of enforcement measures

According to Article 7(3) corrective actions can be taken by operators upon the competent authorities' request following a check that showed irregularities as regards proper implementation of the legal requirements. Pursuant to Article 13 penalties may be imposed for non-compliance. The difference is that corrective actions are requested in the context of implementation whereas penalties in the context of enforcement. As explained in a previous answer this proposal aims at changing the behaviour of timber operators by reducing the incentives for placing illegally harvested timber and timber products on the Community market rather than punishing them. Operational and realistic requirements are thus being proposed to ensure effective implementation which will in turn enable the Community to meet the principal objective of reinforcing its policy as regards illegal logging and associated trade. To underpin this objective it was considered appropriate to introduce the possibility of soft measures to be taken in case of failures to comply with the due diligence requirements before resorting to sanctions. As for penalties the subsidiarity principle requires that the scope and process of the corrective measures will be determined by Member States.

MONITORING ORGANISATIONS

- Who could qualify? Even a company?

Yes, as stated above any entity that satisfied the general requirements as set down in the draft regulation could qualify, including a company, which offer such services on a commercial basis.

- Could a non-EU organisation be recognised?

Under the terms of Article 2 (h) and 5 of the proposal nothing prevents an organisation from outside of the EU to seek recognition in a specific EU MS.

- Where does the automatic/mutual recognition or withdrawal of recognition stem from?

In light of the principle of subsidiarity the granting and withdrawal of recognition of monitoring organisations is left to Member States. It is however important that this national contribution will not result in discrimination and distortion of competition hence undermining the common market. It is therefore crucial that a recognition/withdrawal of a monitoring organisation applies throughout the Community. To ensure the maximum level of consistency, transparency and credibility this recognition throughout the Community should be based on a consultative process whereby all Member States are involved. Paragraph 6 of Article 5 empowers the Commission with the assistance of the Committee and subject to the Councils' and EP scrutiny to lay down the detailed rules that will govern the process of the automatic/mutual recognition.
