

BRIEFING ON PROPOSAL FOR A REGULATION ON DEFORESTATION- FREE PRODUCTS

On 17 November 2021, the European Commission proposed a regulation on deforestation-free products. This proposal falls within the ambit of the European Green Deal which aims to make the EU climate-neutral by 2050 and to curb biodiversity loss. The proposal's objective is to promote products and value chains that exclude deforestation and forest degradation. Here we answer 8 key questions about the EU proposal.

In a separate briefing we address the international context of the EU proposal: its potential World Trade Organization (WTO) implications and similar US and UK regulations. The separate briefing is available [here](#).

1. Why is the EU proposing such a regulation?

According to the European Commission (Commission), the main driver of deforestation and forest degradation is the expansion of agricultural land, which is linked to the production of commodities the EU imports, in particular soya, beef, palm oil, wood, cocoa and coffee. As the EU is a major economy and consumer of these commodities, the Commission considers the EU to be partly responsible for this problem, with this new proposed regulation, aims to minimise EU-driven deforestation and forest degradation.

By promoting the consumption of 'deforestation-free' products and reducing the EU's impact on global deforestation and forest degradation, the Commission expects the proposal to reduce greenhouse gas emissions and reduce biodiversity loss. The Commission estimates projected benefits in the form of more than 71,920 hectares of forest less affected by EU-driven deforestation and forest degradation annually by 2030, and a reduction of at least 31.9 million metric tons of carbon emissions to the atmosphere. The Commission further expects the proposal to contribute to protecting biodiversity which is also strongly linked to preventing climate change.

Key issues

This briefing looks at 8 key questions about the EU proposal:

- 1. Why is the EU proposing such a regulation?
- 2. What is the scope of the proposed regulation?
- 3. What are the main compliance requirements?
- 4. What is the process of identifying risk levels of countries (low, standard, high)?
- 5. How will the requirements of the proposed regulation be enforced?
- 6. Does the proposal provide for transition periods?
- 7. What impact will the proposed regulation have on companies operating in the EU?
- 8. What are the next steps?

2. What is the scope of the proposed regulation?

The proposed regulation applies to six primary commodities (soya, beef, palm oil, wood, cocoa and coffee) but also to products derived from these commodities such as leather, chocolate and wooden furniture. These commodities and derived products have been selected based on scientific data and previous research showing that they contribute the most to global deforestation and forest degradation through European production and consumption.

The proposed regulation would apply to all companies placing these commodities and derived products on the EU market for the first time or exporting them from the EU market.

The key provision of the new proposed regulation is that the covered commodities and derived products may only be placed on or exported from the EU market if they fulfil the following conditions:

- they are deforestation-free (meaning they were produced on land that has not been subject to deforestation after 31st December 2020, and with respect to wood, has been harvested without inducing forest degradation after 31st December 2020); and
- they have been produced in accordance with the relevant legislation of the country of production.

3. What are the main compliance requirements?

To ensure that companies comply with the conditions of products being deforestation-free and in line with the laws of the country of origin, companies will be obliged to conduct ongoing due diligence.

As a first step, companies would need to collect information and documents on (inter alia) the commodity/product, quantity, supplier, country of production and geo-location coordinates of all plots where the products were produced. As deforestation is linked to land-use change, monitoring deforestation requires a precise link between the product and the plot of land where it was grown. Therefore, obtaining geo-location coordinates is crucial for monitoring deforestation (regarding checks by authorities, see question 5).

Based on the collected information, companies are then required to conduct a risk assessment analysing and evaluating whether products are compliant with the requirements of the new proposed regulation. For this risk assessment, the proposed regulation sets risk assessment criteria. These include (inter alia) the presence of forests in the country and area of production, prevalence of deforestation or forest degradation in the country/region/area of production, the complexity of the relevant supply chain, and, in particular, the difficulties of connecting products to the plot of land where they were produced, or the risk of mixing with products of unknown origin or production in deforested areas.

In cases where they identify a non-negligible risk (showing cause for concern) of non-compliance with the requirements of the proposed regulation, companies are required to adopt risk mitigation measures (the third step of due diligence) which are adequate to remove the risk or reduce it to a negligible level. Such risk mitigation measures can include requiring additional information, data or documents or undertaking independent surveys or audits.

If companies cannot demonstrate the absence of risk or negligible risk, they must not place the relevant products on the EU market or export them.

In cases where due diligence results in a company concluding that there is no risk or only a negligible risk of non-compliance with the requirements of the proposed regulation, the company will be required to submit a due diligence statement to the competent authority (designated within each Member State, regarding the role of competent authorities, see question 5 below) via an official EU information system.

On an ongoing basis companies must establish a due diligence system to manage the relevant due diligence steps and keep it up to date. In this respect, they must also publicly report on their due diligence systems.

Companies have the option of undertaking a simplified due diligence exercise (limited to the collection of information and documents) where they can ascertain that all products have been produced in low-risk countries or parts thereof. Regarding the process of identifying risk levels of countries, please refer to the next question 4.

4. What is the process of identifying risk levels of countries (low, standard, high)?

After the entry into force of the proposed regulation, the European Commission will assess risk of countries based on the mentioned assessment criteria, will decide on the countries' risk levels in due course and will publish the risk levels of countries in a publicly available list. Generally, the Commission can identify countries as having a low, standard or high risk of producing goods that are not compliant with the proposed regulation - thus triggering different levels of scrutiny. The proposed regulation provides for a variety of assessment criteria in this respect, such as (inter alia) the rate of deforestation and forest degradation, rate of expansion of agriculture land for relevant products or whether NDCs under the Paris Agreement cover emissions and removals from agriculture, forestry and land use. The objective of this benchmarking system is to incentivise countries to ensure stronger forest protection and governance and to facilitate trade.

Products from high risk countries would be subject to enhanced scrutiny by competent authorities of Member States (regarding the role of competent authorities, see question 5 below). Where this applies, competent authorities need to ensure that the checks they carry out on an annual basis are covering at least 15% of companies (placing on or exporting from the EU market products from high risk countries) and 15% of the quantity of relevant products produced in high-risk countries or parts thereof.

For standard and low risk countries, competent authorities need to carry out checks on an annual basis but are only obligated to cover at least 5 % of companies as well as 5 % of the quantity of relevant products (regarding checks by authorities, see question 5). Only for products from low-risk countries or parts thereof, companies have the option of a simplified due diligence exercise (limited to the collection of information and documents). At the entry into force of the proposed regulation, all countries will be assigned a standard level of risk.

5. How will the requirements of the proposed regulation be enforced?

Member States will be required to designate one or more competent authorities responsible for carrying out the obligations imposed on them by the proposed regulation. The designated competent authorities would have the obligation to check corporate compliance and whether products are compliant with it. Checks on companies will include, inter alia, examinations of their due diligence systems and due diligence statements as well as documentation and records maintained by companies that demonstrate the compliance of products with the requirements of the proposed regulation. Checks can also include, where appropriate, any technical and scientific means adequate to determine whether the relevant product is deforestation-free (such as Earth observation data or field audits). Based on the risk level of countries, checks need to cover companies and quantities of products from at least 5 % to 15 % under enhanced scrutiny.

Most importantly, under the proposed regulation competent authorities can require companies to take the following actions (inter alia):

- prevent the relevant products from being placed, made available on or exported from the EU market,
- withdraw or recall the product immediately, and/or
- destroy the relevant product or donate it to charitable or public interest purposes.

As a further enforcement measure, Member States will be able to impose penalties for infringements of the proposed regulation, such as fines, confiscation of products, confiscation of revenues and temporary exclusion from public procurement processes.

6. Does the proposal provide for transition periods?

Yes. The main obligations for both companies and competent authorities will apply twelve months from the entry into force of the proposed regulation. Microbusinesses (businesses with total asset value of maximum EUR 350.000,00, net turnover of maximum EUR 700.000,00 and an average number of employees during the financial year of 10 or fewer, established by 31 December 2020) will be given an extra year.

7. What impact will the proposed regulation have on companies operating in the EU?

The proposed regulation sets common rules for any company - from within the EU or from outside - placing products on the EU market or exporting from the EU. It aims to ensure that domestic and imported commodities are measured by the same standards.

The Commission concludes that the shift towards sourcing deforestation-free products will likely place a burden on companies, for example when producing in countries such as Indonesia and Malaysia (as, for example, palm oil represents the countries' second and fifth highest value export respectively). The due diligence requirements of the proposed regulation are likely to

increase costs. However, the transition periods (see question 6) give companies time to adequately adjust to the new requirements of the proposed regulation. Moreover, the Commission expects the demand for deforestation-free products to grow in the EU and thereby boost sustainable businesses and business models across the world.

In addition, the Commission will establish specific cooperation programmes, such as forest partnerships, with countries. The forest partnerships' main objective will be to protect, restore and/or ensure the sustainable use of forest in a comprehensive and integrated way to help countries comply with the proposed regulation. They will promote forest governance and policy reforms to pursue sustainable forest management and contribute to halting deforestation and forest degradation.

8. What are the next steps?

The proposed regulation will now pass to the European Parliament and Council for adoption according to the ordinary legislative procedure. It is always difficult to predict the length of time required for Parliament and Council to reach consensus but it is likely to take between 18 months and two to three years (between June 2023 and the end of 2023 or 2024 for example).

The Commission has decided to implement the proposal in the (legal) form of an EU Regulation meaning that it will be directly applicable as soon as it comes into force, rather than dependent on individual Member States bringing it into force. This will reduce the likelihood of divergence between Member States in the application and enforcement of the regime.

After the entry into force of the proposed regulation, transition periods apply (see question 6). After the entry into force of the proposed regulation the Commission will assess the risk of non-compliance in countries and will determine the risk-level of countries according to its benchmarking system (see question 4).

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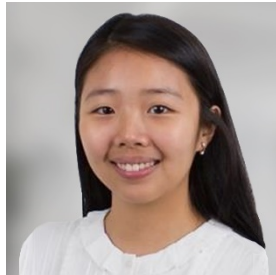
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