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The EPP's Proposed Amendments to EUDR: Why the 'insignificant risk' category and trader exemptions open up series of loopholes

1. Proposal for an insignificant risk category

The European People's Party (EPP) has proposed a series of amendments to the EU Regulation on Deforestation-Free Products (EUDR) that would significantly reduce its effectiveness and dramatically hinder enforcement. One of these proposals is for a new benchmarking category that would allow countries or parts of countries to be classified as 'no-risk' or 'insignificant risk.' Currently, the benchmarking process under the EUDR would only classify countries as low, standard or high risk.

EPP's proposed 'insignificant risk' countries or areas would meet the following criteria:

- Forest area development remained stable or increased compared to 1990;
- Paris Climate Agreement and international conventions on human rights and preventing deforestation are signed by countries and parts thereof;
- Enforced regulations on preventing deforestation and forest conservation at national level are strictly implemented in full transparency and monitored.

Operators or traders sourcing relevant goods from an insignificant risk country or area would no longer need to comply with the zero-deforestation requirement in the law.

They would also be exempt from providing a due diligence statement (DDS), with its associated geolocation requirements. Instead operators sourcing relevant goods from insignificant risk areas would keep documentation relating to the trade name, type and quantity of the relevant products, the country of production, business information and "adequately conclusive and verifiable information" that the products are free from forest degradation and produced in accordance with the relevant legislation in the country of production.

1.1 The proposed definition of 'insignificant-risk' is carelessly drafted and ambiguous

The proposed amendments use the terms 'no risk' and 'insignificant-risk' interchangeably, which leads to confusion and contradicts the intent of Article 4. The due diligence process outlined in Article 4 requires evidence that there is no non-negligible risk of deforestation or forest degradation.

Two of the proposed criteria for classifying countries as insignificant-risk raise major potential problems:

- *Forest area development remained stable or increased compared to 1990*;

The proposed criterion seems to be drawn from an article by the European Forest Institute stating that forest area in the EU increased by 10 per cent (14 million hectares) from 1990 to 2020.

Applying this standard could effectively exempt all 27 EU countries (see figure from EFI article below), raising concerns about discrimination against producer countries. Such an approach might also violate the WTO principles of trade without discrimination.

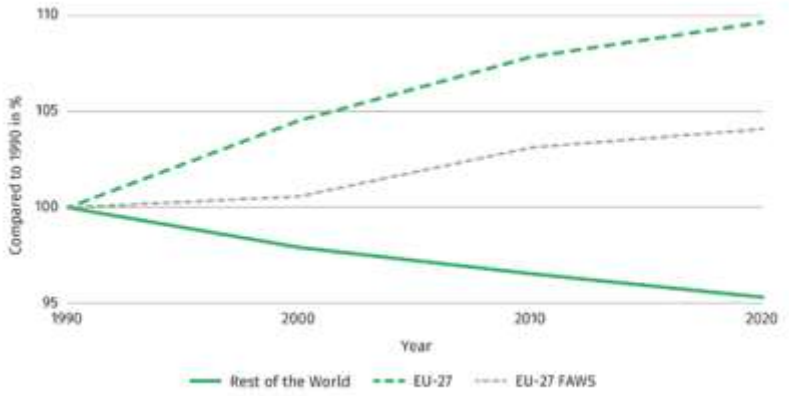


Figure 2: Development of Forest Area 1990-2020 (index for 1990 = 100).

Furthermore, an increase in forest cover does not guarantee that forest activities are legal or environmentally sustainable. There is significant commercial logging activity in European forests - the EU's own statistics show that 65% of the annual wood increment in EU forests was removed by the logging industry in 2021, with Czechia and Germany exceeding 90% of the net increment. Some of this activity takes place in old growth forests - between 2003 and 2019, 20% of all the clear-cut forest in Sweden was old-growth.

- *Paris Climate Agreement and international conventions on human rights and preventing deforestation are signed by countries and parts there of;*

The Paris Climate Agreement, signed by 194 countries and the EU, covers nearly every country. Including this as an exemption criterion would allow almost every country to bypass the regulation. Similarly, the fact that most countries have signed 18 International Human Rights Treaties does not guarantee that they are enforcing meaningful protections on human rights and preventing deforestation. Additionally, it is not clear whether the term 'international conventions' is intended to include the Glasgow Leaders Declaration on Forests and Land Use, the New York Declaration on Forests or the Amsterdam Declaration Partnership.

Lastly, the proposed amendment lacks clarity about whether countries must meet all three proposed criteria to be classified as insignificant-risk.

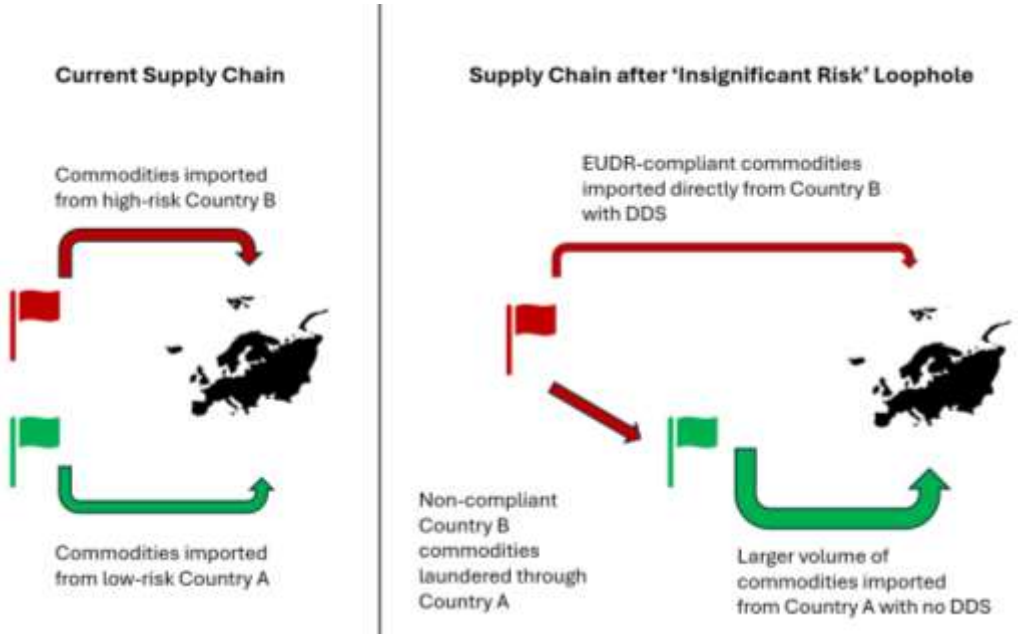
1.2 Exempting insignificant-risk supply chains from due diligence would open up a massive loophole

If the EPP's proposed amendments are accepted, operators and traders would be able to place commodities on the market without a DDS or without providing geolocation coordinates if those products were produced in an insignificant-risk country. While the wording of the proposed amendments is vague, this is likely intended to mean that products grown or harvested in insignificant-risk countries are exempt from the requirement for a DDS. (Although see below for an alternative interpretation.)

This could lead to laundering of non-compliant commodities through insignificant-risk countries.

Say, for example, that Country A is insignificant-risk under EUDR. Sawn timber from Country A could be placed on the market without the operator lodging a DDS. That wood would continue making its way through supply chains – as flooring, furniture or other wood products - without being linked to a DDS or geolocation coordinates.

This would provide an opportunity for suppliers from standard- or high-risk countries whose timber would not meet EUDR requirements to reroute their wood through Country A to evade the regulations. Once timber is processed in Country A its origin could be easily lost or disguised. With no ability to check geolocation coordinates, a Competent Authority would struggle to identify whether the product has genuinely originated in Country A.



1.3 This approach is already used to circumvent EUTR and trade sanctions

There is already evidence of companies changing trade routes to evade tariffs and sanctions. Earlier this year, a European Commission investigation found evidence of plywood made in Russia being laundered and re-labelled as of Kazakh or Turkish origin to evade higher tariffs imposed on Russian wood products. Earthsight's analysis of the Commission's research showed that illegal ply with a retail value of some €14.4m was flooding into Europe from Turkey and Kazakhstan every month.

There is also evidence of operators attempting to circumvent the EUTR by placing illegal wood products on the EU market in countries thought to have weaker enforcement. For example, in 2020 the Environmental Investigation Agency exposed how companies rerouted trade once Myanmar teak was deemed non-compliant with EUTR, shifting trade away from countries that had taken enforcement actions. The investigation documented non-compliant Myanmar teak coming into Croatia, which had a reputation for less stringent EUTR enforcement, with the intention of then being sold into other parts of Europe.

Misrepresentation of the origin of wood is common in timber supply chains. A forensic wood anatomy analysis of 73 wood products in the US found 45 of them (62 per cent) had one or more fraudulent or misrepresented claim. A similar study in Australia found that 25 per cent of timber products tested in a government-funded study had misdeclared the species, origin or both.

Similar issues have been found in non-timber commodity supply chains. The UK government has accused businesses importing goods from the EU of making deliberate errors on import documentation to circumvent Brexit border charges. Importers have been found listing 'high risk' products as 'medium risk' and medium risk as low risk to avoid checks. A 2021 investigation also found widespread mislabelling of the origin of cotton products for sale in the US. An exemption that relies on accurate labelling of country of origin is ripe for exploitation.

The requirement for all products to come with geolocation coordinates is designed to help Competent Authorities to identify these kinds of evasive actions. For example, if a Competent Authority identifies a suspicious increase in a commodity coming from a low- or insignificant-risk country, it can review the geolocation coordinates in each DDS to determine where exactly it was harvested. If an implausibly large volume is coming from a single plantation, this would be a red flag requiring a more thorough investigation.

1.4 Vague wording raises an even higher risk

The wording of the proposed amendments is vague – referring to 'products from' insignificant-risk countries. This raises the prospect of an even higher risk – that the exemption from due diligence would apply to products *imported from* or *processed in* an insignificant-risk country – not just those grown or harvested in an insignificant-risk country. While this does not appear to be the intention of the amendments, unclear drafting in this important area raises confusion for businesses and regulators which could have unintended consequences if they are misinterpreted.

Many products with a high risk of causing deforestation are likely to enter the EU via an insignificant-risk country. For example, since there is no major deforestation for relevant commodities within the country, Switzerland is likely to be deemed insignificant-risk under the EPP's proposed benchmarking criteria. Switzerland exports almost as much coffee (€1.4bn) to the EU as Vietnam (€1.5bn), and far more than major producer countries Honduras, Colombia and Guatemala. It is the third largest supplier overall. Removing traceability requirements for imports from Switzerland would therefore create a loophole that could allow products from high-risk countries to enter the EU without due diligence or the need to comply with the no-deforestation requirement.

It would also penalise non-OECD producer countries (which are more likely to be classified standard or high risk and still need traceability) and benefit the, mostly wealthier, secondary processing and re-exporting countries (which are more likely to be insignificant-risk). Producer countries are already at pains to try to move more of the added-value processing of these commodities into their own territories. The effect of giving products which reach the EU via third parties a 'pass' would be to further undermine those efforts.

2. Exemption for large traders

If accepted, the EPP's proposals would also exempt large traders from many of the due diligence requirements under the EUDR. Traders are the downstream businesses – such as supermarkets or retailers – who sell products covered by the EUDR but are not the first ones to place the product on the EU market. SME traders already have such an exemption.

As with the exemption for insignificant-risk countries, the exemption of traders from the law is not clearly expressed and there would be substantial implementation challenges should the proposed amendments go ahead in their current form. For example, it is unclear from the framing of the proposed amendment whether the intention is to exempt all traders from all substantive requirements of the law, or to apply the current requirements for SME traders to all traders.

If the latter, under the proposed exemption, traders would be required to keep basic information about the products they are selling and act if they are made aware that something they are selling does not comply with the EUDR. They would not be required to lodge a DDS or undertake substantial due diligence.

2.1 Due diligence for large traders is an important safeguard

Removing due diligence for large traders rests on the false assumption that every operator will carry out its obligations under the regulation dutifully and without error, that due diligence statements submitted by operators are proof of compliance, and that enforcement mechanisms will work flawlessly. Experience with the EUTR shows that this is far from the truth.

Firstly, weak EUTR enforcement in some Member States created massive loopholes for operators placing illegal wood products on the EU market in those countries, letting traders further downstream off the hook since they were not subject to any due diligence requirements (see 1.3, above).

Secondly, operators may set up shell companies, which if caught in breach of the law can simply declare bankruptcy and potentially avoid penalties. In 2018, Earthsight revealed how many of the biggest importers of Ukrainian wood in Europe were circumventing the regulation and avoiding their obligations by establishing small shell firms in Member States with weak enforcement, including one registered at a flat above a shop in a small village in eastern Poland. Under the EUDR, due diligence requirements have been extended to traders specifically as an attempt to remedy these known circumvention loopholes and enforcement challenges, which were laid bare in the EUTR fitness check.

Removing due diligence obligations on traders removes an important tool that Competent Authorities can use to hold non-compliant companies accountable. It also provides an unjustified exemption for companies that trade large volumes of commodities and should have systems in place to ensure the goods they sell are EUDR compliant.

3. Recommendation

Members of the European Parliament should vote against all proposed amendments and ensure the EUDR is implemented in its current form.

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