

## Summary: Intervention & Options

<b>Department /Agency:</b> DEFRA	<b>Title:</b> Public Consultation on the European Commission's Proposal for a Due Diligence Regulation, and the amendments adopted by the European Parliament Committee on Environment, Public Health and Food Safety.
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**Stage:** Negotiation

**Version:** 1

**Date:** 01/04/2009

### Related Publications

- 5036/09 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
- SEC(2008) 2616 / 14482/08 ADD 1 Commission Staff working document accompanying the Proposal – Summary of the Impact Assessment Report on additional options to combat illegal logging
- European Parliament Committee on Environment, Public Health and Food Safety compromise and consolidated amendments to the Proposed Regulation<sup>1</sup>

**Available to view or download at:**

<http://www.defra.gov.uk/corporate/consult/DDR/index.htm>

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<sup>1</sup> [http://www.europarl.europa.eu/meetdocs/2004\\_2009/documents/dv/769/769103/769103en.pdf](http://www.europarl.europa.eu/meetdocs/2004_2009/documents/dv/769/769103/769103en.pdf)

## What is the problem under consideration? Why is government intervention necessary?

The UK government has a longstanding commitment to tackling illegal logging. The causes of the problem of illegal logging can be attributed broadly to failure of international markets, which continue to accept illegal timber products, and failures of governance which allow commercial and political elites to benefit from forest exploitation by evading national forest laws in producer countries. Continued deforestation is a significant contributor to global carbon emissions, with deforestation accounting for approximately 18% of global emissions.

Consumer countries have a key role in putting in place policies to control the flow of illegal timber into the EU. As we are seeking a trade-based solution to illegal logging, efforts are most effective when taken at the EU level.

A significant element of the EU's 2003 Forest Law Enforcement, Governance and Trade (FLEGT) Action Plan is negotiation and implementation of Voluntary Partnership Agreements (VPAs) with timber producing countries where illegal logging is a recognised problem. These VPAs will establish a licensing system which ensures that exports of timber products to the EU have been legally harvested. However, it is recognised that VPA coverage will be incomplete and that additional measures are required to prevent imports of illegally harvested timber into the EU. The European Commission reviewed a number of options for additional EU legislation, and in October 2008 published their Proposal for the timber 'Due Diligence Regulation' (DDR). The proposal requires operators first placing timber and timber products on the Community market to exercise due diligence, using a risk-based approach, to minimise the risk of placing illegal timber or timber products on the Community market.

On 17 February 2009, the European Parliament's Committee on Environment, Public Health and Food Safety adopted 75 compromise and consolidated amendments to the proposal, including the introduction of a requirement that operators place or make available on the market only legally harvested timber or timber products, at all points in Community market supply chains: in effect a prohibition on selling illegal products. The amendments also proposed concentrating more regulatory oversight with the Commission. The Parliament will vote on these amendments on 23 April 2009.

The UK has also been evaluating the merits of the Proposal and its expected impact on illegal logging. As a result of these deliberations, and **subject to the responses received on this public consultation, we are currently minded to seek the inclusion of a prohibition on placing illegally harvested timber on the Community market.** We believe that making it an offence to place illegally harvested timber on the Community market could strengthen the Regulation, and send a clear message to operators that such activity was no longer acceptable, creating a level playing field for importers across the EU. It would also enable enforcement authorities to take action where evidence of the trade in illegal timber had been brought to their attention. However, the UK believes that such a prohibition should apply only to operators who first place timber or timber products on the Community market, and that the onus on proving such an offence should remain with the authorities.

### What are the policy objectives and the intended effects?

The intended objective of the current Commission proposal is to reduce the volume of illegal timber entering the EU, and to change operator behaviour in sourcing timber products by requiring operators to check that the products they sell have been legally harvested.

Operators will be required to apply a risk-based approach to removing timber harvested in contravention to the laws of the country of origin from their supply chains. Operators placing timber and timber products for the first time on the Community market should exercise due diligence through a system of measures and procedures (i.e. a due diligence system) to minimise the risk of placing illegally harvested timber and timber products on the Community market. Operators are defined as any natural or legal person that places timber or timber products on the market – this could be forest owners, agents or importers of timber and timber products. The Commission's proposed Regulation only applies to those operators who place timber or timber products on the Community market for the first time.

To ensure compatibility with WTO rules on non-discrimination, the Proposal will apply to the whole trade, including European (and thus UK) producers of timber.

What policy options have been considered? Please justify any preferred option.

The European Commission reviewed 5 different options for additional legislative measures while developing the Due Diligence Regulation, ranging from voluntary measures to an outright ban on trade in illegal timber. The Commission subsequently chose a **6<sup>th</sup> option** - the Due Diligence approach. The European Commission Proposal suggests that a major benefit of the option it chose, **Option 6**, is that it will tend to favour sourcing from countries with reliable forest management practices, including those which have signed VPAs and will therefore export FLEGT-licensed timber products to the EU.

The Commission estimate that costs are proportionate to the need for the Community to improve the efficiency of its policy against illegal logging and the related trade. This approach also means that over time, operators will benefit from the elimination of illegal timber products from the market. The chosen option is also seen to require the smallest additional administrative burden of the 6 proposals considered, as it seeks to build on existing good practice in the industry across the EU on chain of custody monitoring. UK industry is recognised as a leader in the area of developing supply chain management and legality verification systems.

Following the Commission's choice of the 6<sup>th</sup> option, the UK Government has developed three scenarios to illustrate what a national framework for due diligence systems might look like in the UK. **These scenarios are meant to illustrate a range of potential cost levels associated with implementing the Regulation in the UK, but cannot be considered exhaustive and complete assessment of potential costs.** The three scenarios have been outlined at section 4.3. We have included these three scenarios as the basis for indicative costs.

Of particular note is the lack of sufficient data on what proportion of those in the timber Industry are involved in 'first placing' timber on the Community market for different Industry sectors. There is also insufficient data on the proportion of those in the timber industry that already have due diligence processes in place. The 3 Scenarios have thus made an assumption of the level of companies who would be in scope of the Regulation . **We have performed a further analysis of potential costs for Scenario 2, to illustrate the likely range of costs associated with meeting the Regulation under lower assumptions of the level of manufacturing and retail companies engaged in first placing on the Community Market.** We have some data to support this additional analysis, but this is presented as a guide only, and illustrates the potentially range of costs that could be associated with the final Regulation.

We have also included provision for a possible prohibition on the placing of illegally harvested timber on the Community market for the first time. We expect that the only additional costs emerging from this proposition would be the costs of prosecuting those who have demonstrably traded illegal timber under this specific prohibition, and so the addition of a prohibition would not change the order of costs outlined in the scenarios below.

The draft Regulation is intended as a broad framework, to be supplemented by more detailed implementation requirements, after agreement of the initial Regulation. As such, the Proposal does not provide comprehensive detail on how individual organisations must comply with the risk assessment processes. The Commission has indicated that:

**“Further details will be laid down by way of implementing measures in order to facilitate implementation, notably with respect to the identification of the criteria for determining the presence of a high or low risk that illegally harvested timber and timber products are placed on the Community market. In laying down those implementing measures the following principles should be respected: the need to avoid putting any unnecessary burden on the operators; the balance of costs and benefits to operators covered by this Regulation; the need to respect the necessary flexibility in the application of the implementing measures; the need to facilitate the adaptation of small operators to the requirements laid down in this Regulation.”**

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

The UK will be seeking a review clause in the Regulation to ensure the effects of the policy can be monitored and revised if necessary.

**Ministerial Sign-off** For Consultation Impact Assessment ahead of a Public Consultation:

*I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.*

Signed by the responsible Minister:

..... Date:

## Summary: Analysis & Evidence

<b>Scenario: 1</b>	<b>Description: Due diligence systems based on operators' self-declaration, but not third-party audited</b>
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<b>COSTS</b>	<b>ANNUAL COSTS</b>	Administrative cost increases will be spread across all importers of wood. Costs to wood producers in the UK are not expected to rise significantly.
	<b>One-off</b> (Transition) <span style="float: right;">Yrs</span>	
	£ 2.03m <span style="float: right;">1</span>	
	<b>Average Annual Cost</b> (excluding one-off)	
	£ 11.90m	
<b>Total Cost (PV)</b>		£ 35.37m
Other <b>key non-monetised costs</b> by 'main affected groups'		
There will be additional enforcement costs to government where prosecutions are brought against operators suspected of trading in illegal timber.		

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>	These monetised benefits will accrue <b>internationally</b> ; they represent a share of losses incurred by governments and the wider economy of forest nations as a result of the illegal trade. That could be reduced if illegal logging is reduced. Further details are discussed in the evidence base. (Range assumes 50%-100% efficacy of policy in reducing share of illegal logging attributed to the UK – best estimate used in this scenario is 50%)
	<b>One-off</b> <span style="float: right;">Yrs</span>	
	£ <span style="float: right;"></span>	
	<b>Average Annual Benefit</b> (excluding one-off)	
	£212.5m-425m	
<b>Total Benefit (PV)</b>		£ 595-1,191m
Other <b>key non-monetised benefits</b> by 'main affected groups' – the impacts of reduced illegal logging on overall rates of deforestation, there are significant local and global benefits of reduced deforestation, including carbon emissions reduction and biodiversity protection.		

- **Key Assumptions/Sensitivities/Risks** We assume that a certain proportion of companies are already operating some form of due diligence system. The assessment of how many was based on the current level of legality assurance in particular sectors, and extended to other sectors where information is lacking.
- Scenario 1 could not separate those companies who first place timber on the market from those involved in the timber trade more generally, due to lack of data. As such, our assessment of the number of possible companies in scope of the Regulation is based on information from industry sources, and hence the costs associated with the Regulation could likely to be inflated .
- In particular, the furniture industry figures are difficult to assess , due to its current uptake of legality certified product ,the disaggregation of the sector , and the number of companies specifically involved in first placing on the market is largely unknown.
- We also assume that the existing systems already on the market for legality verification and forest management practices will be capable of meeting the requirements of the Regulation.

Price Base Year 07/08	Time Period Years 3	<b>Net Benefit Range (NPV)</b> £ 560m-1,155m	<b>NET BENEFIT (NPV Best estimate)</b> £560m
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What is the geographic coverage of the policy/option?		EC measure with global effect		
On what date will the policy be implemented?		2 yrs after entry into force		
Which organisation(s) will enforce the policy?		HMG (to be agreed)		
What is the total annual cost of enforcement for these organisations?		£ unknown		
Does enforcement comply with Hampton principles?		yes		
Will implementation go beyond minimum EU requirements?		no		
What is the value of the proposed offsetting measure per year?		£ not yet considered		
What is the value of changes in greenhouse gas emissions?		£ not yet quantified		
Will the Proposal have a significant impact on competition?		Potentially.		
Annual cost (£-£) per organisation(excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	Under	Under	N/A	N/A

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)		(Increase - Decrease)	
Increase of £ 11.14m	Decrease of £	<b>Net Impact</b>	£ 11.14m

Key:

Annual costs and benefits: Constant Prices

(Net) Present Value

## Summary: Analysis & Evidence

<b>Scenario: 2</b>	<b>Description: Scenario 2: an elevated version of the current systems used by trade associations such as the UK Timber Trade Federation (TTF), that have responsible purchasing policies, combined with the mode of operation of the UK Central Point of Expertise on Timber (CPET) . This scenario assumes that products originating from low-risk countries use a form of self-declaration. All other countries of origin would require the purchase of third-party verification material. All companies would need to be third-party audited. This scenario is similar to existing practice for timber importers.</b>
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<b>COSTS</b>	<b>ANNUAL COSTS</b>		Administrative cost increases will be spread across all importers of wood. Additional due diligence cost will be borne predominately by producers importing wood from high risk countries outside the EU. Costs to wood producers in the UK are not expected to rise significantly. <b>NOTE: A range for the one-off costs is shown in this scenario as a further analysis has been performed to account for a different assumption of the proportion of companies which are first placers on the market. The centre of this range has been taken as the best estimate.</b>
	<b>One-off (Transition)</b>	<b>Yrs</b>	
	£ 2.1-6.4m	1	
	<b>Average Annual Cost</b> (excluding one-off)		
	£ 160.6-188.2m	<b>Total Cost (PV)</b>	£452m - 534m
<p><b>Other key non-monetised costs by 'main affected groups'</b></p> <p>There will be additional enforcement costs to government where prosecutions are brought against operators suspected of trading in illegal timber.</p>			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' These monetised benefits will accrue <b>internationally</b> , they represent a share of losses incurred by governments and the wider economy of forest nations as a result of the illegal trade. That could be reduced if illegal logging is reduced. Further details are discussed in the evidence base. (Range assumes 50%-100% efficacy of policy in reducing share of illegal logging attributed to the UK – best estimate used in this scenario is 75%)
	<b>One-off</b>	<b>Yrs</b>	
	£		
	<b>Average Annual Benefit</b> (excluding one-off)		
	£ 212.5m-425m	<b>Total Benefit (PV)</b>	£ 595-1,191m
<p><b>Other key non-monetised benefits by 'main affected groups'</b> – the impacts of reduced illegal logging on overall rates of deforestation, there are significant local and global benefits of reduced deforestation, including carbon emissions reduction and biodiversity protection.</p>			

### Key Assumptions/Sensitivities/Risks

- That a certain proportion of companies are already operating some form of due diligence system. The assessment of how many was based on the current level of legality assurance in particular sectors, and extended to other sectors where information is lacking.
- For this Scenario, we have taken forward an additional assessment which assumes a further range

of the number of companies who are involved in first placing timber on the Community market. Details of the assumption levels used is in Annex 5.

- We also assume that the existing systems already on the market for legality verification and forest management practices will be capable of meeting the requirements of the Regulation.

Price Base Year 08/08	Time Period Years 3	<b>Net Benefit Range</b> (NPV) £ 61m – 739m	<b>NET BENEFIT</b> (NPV Best estimate) £ 400m
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What is the geographic coverage of the policy/option?		EC measure with global effect		
On what date will the policy be implemented?		2 yrs after entry into force		
Which organisation(s) will enforce the policy?		HMG (to be agreed)		
What is the total annual cost of enforcement for these organisations?		£ unknown		
Does enforcement comply with Hampton principles?		yes		
Will implementation go beyond minimum EU requirements?		no		
What is the value of the proposed offsetting measure per year?		£ not yet considered		
What is the value of changes in greenhouse gas emissions?		£ not yet quantified		
Will the Proposal have a significant impact on competition?		Potentially.		
Annual cost (£-£) per organisation	Micro	Small	Medium	Large
Are any of these organisations exempt?	Under	Under	N/A	N/A

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)		(Increase - Decrease)	
Increase of £ 13.1m-38.9m	Decrease of £	<b>Net Impact</b>	<b>£13.m-38.9m</b>

Key:

Annual costs and benefits: Constant Prices

(Net) Present Value

## Summary: Analysis & Evidence

Policy Option: 3

Description: Scenario 3: includes third-party auditing, with verified third-party legal timber as the minimum requirement (whether domestically grown or originating outside the EU).

COSTS	ANNUAL COSTS		Administrative cost increases will be spread across all importers of wood. Additional due diligence cost will be placed on all importers of wood from within the EU and high and low risk countries outside of the EU. Costs to wood producers in the UK are not expected to rise significantly.
	One-off (Transition)	Yrs	
	£ 13.14m	1	
	Average Annual Cost (excluding one-off)		
£ 255.90m		<b>Total Cost (PV)</b>	£ 730.08m
Other <b>key non-monetised costs</b> by 'main affected groups'			
There will be additional enforcement costs to government where prosecutions are brought against operators suspected of trading in illegal timber.			

BENEFITS	ANNUAL BENEFITS		Description and scale of <b>key monetised benefits</b> by 'main affected groups' These monetised benefits will accrue <b>internationally</b> , they represent a share of losses incurred by governments and the wider economy of forest nations as a result of the illegal trade. That could be reduced if illegal logging is reduced. Further details are discussed in the evidence base. (Range assumes 50%-100% efficacy of policy in reducing share of illegal logging attributed to the UK – best estimate used in this scenario is 100%)
	One-off	Yrs	
	£		
	Average Annual Benefit (excluding one-off)		
£ 212.5m-425m		<b>Total Benefit (PV)</b>	£ 595-1,191m
Other <b>key non-monetised benefits</b> by 'main affected groups' – the impacts of reduced illegal logging on overall rates of deforestation, there are significant local and global benefits of reduced deforestation, including carbon emissions reduction and biodiversity protection.			

### Key Assumptions/Sensitivities/Risks

- We assume that a certain proportion of companies are already operating some form of due diligence system. The assessment of how many was based on the current level of legality assurance in particular sectors, and extended to other sectors where information is lacking.
- Scenario 3 could not separate those companies who first place timber on the market from those involved in the timber trade more generally, due to lack of data. As such, our assessment of the number of possible companies in scope of the Regulation is based on information from industry sources, and hence the costs associated with the Regulation could likely to be inflated .
- In particular, the furniture industry figures are difficult to assess, due to its current uptake of legality certified product, the disaggregation of the sector , and the number of companies specifically involved in first placing on the market is largely unknown.
- We also assume that the existing systems already on the market for legality verification and forest management practices will be capable of meeting the requirements of the Regulation.

Price Base Year 07/08	Time Period Years 3	<b>Net Benefit Range (NPV)</b> £ -135m to 461m	<b>NET BENEFIT (NPV Best estimate)</b> £ 460.62m
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What is the geographic coverage of the policy/option?	EC measure with global effect			
On what date will the policy be implemented?	2 yrs after entry into force			
Which organisation(s) will enforce the policy?	HMG (to be agreed)			
What is the total annual cost of enforcement for these	£ unknown			
Does enforcement comply with Hampton principles?	yes			
Will implementation go beyond minimum EU requirements?	no			
What is the value of the proposed offsetting measure per year?	£ not yet considered			
What is the value of changes in greenhouse gas emissions?	£ not yet quantified			
Will the Proposal have a significant impact on competition?	Potentially.			
Annual cost (£-£) per organisation	Micro	Small	Medium	Large
Are any of these organisations exempt?	Under discussion	Under	N/A	N/A

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)		(Increase - Decrease)	
Increase of £ 18.34m	Decrease of £	<b>Net Impact</b>	£ 18.34m

Key:

Annual costs and benefits: Constant Prices	(Net) Present Value
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# 1. Proposal

## Background

1.1 The UK government has a longstanding commitment to tackling illegal logging. The causes of the problem are complex but can be attributed broadly to failure of international markets, which continue to accept illegal timber products, and failures of governance allowing commercial and political elites to benefit from forest exploitation by evading national forest laws. The intended action by the EU to target this complex problem is captured in the **Forest Law Enforcement Governance and Trade (FLEGT) Action Plan**, which seeks to address the problem of illegal logging and its related trade through a combination of supply and demand side measures.

1.2 In December 2005, under the UK's Presidency, the Council of Ministers of the European Union adopted the Forest Law Enforcement, Governance and Trade (FLEGT) Regulation. The basis of the Regulation is a licensing scheme, under which the EU enters into binding Voluntary Partnership Agreements (VPAs) with timber producing countries. The Agreements will provide technical assistance to exporting countries to establish a legality assurance system for timber exports. When the scheme is operational in a partner country, unlicensed timber will be denied entry to the Community market. Ghana signed a VPA with the EU in September 2008. Indonesia, Malaysia, Cameroon, Congo Brazzaville and Liberia are currently negotiating agreements, and several other countries have indicated their intent to start negotiations in 2009.

1.3 The FLEGT Action Plan recognises that some important timber-producing countries may choose not to enter into FLEGT VPAs with the EU and therefore that **additional measures are required to prevent imports of illegally harvested timber into the EU.**

1.4 The UK is committed to sustainable forest management domestically and globally. We contribute actively on international forest policy development, and we seek ways of improving forest management. Improving forest governance and ensuring legality is the foundation for sustainability.

## Current Proposal

1.5 The European Commission reviewed a number of options for strengthening the FLEGT Action Plan and controlling the entry of illegal timber into the Community market. The Commission produced an impact assessment which reviewed five different policy options, ranging from voluntary measures, to an outright prohibition on the trade in illegal timber. It then considered an additional (sixth) policy option, and in October 2008, adopted a Proposal for a new **timber Due Diligence Regulation (DDR).**

1.6 The essence of the proposed Regulation is a requirement that traders who first place timber and timber products on the Community market exercise due diligence to minimise the risk that the products they trade have been produced illegally. This will require the implementation of systems for assessing the risk that imports of timber or timber products contain, or are derived from, illegally harvested timber. This will include, where appropriate,

means for verifying the legality of high risk timber, by checking that the timber has been produced in compliance with relevant laws in the country where it was harvested. Timber placed on the market which has been produced in accordance with a Voluntary Partnership Agreement (VPA), or has a valid CITES licence, is to be considered as having been legally harvested.

1.7 Following release of the proposed Due Diligence Regulation, the European Parliament Committee on Environment, Public Health and Food Safety released over 200 amendments to the Regulation, which have been reduced to 75 consolidated and compromise amendments. These were adopted on the 17 February 2009 and will be voted on by the European Parliament on 23 April.

1.8 The UK has considered these amendments and, mindful of ongoing negotiations, **we also wish to seek views from consultees on the possible inclusion of a prohibition on placing illegally harvested timber and timber products on the Community market, at the time of their first placing on the market.**

1.9 To ensure compatibility with WTO rules on non-discrimination, the Proposal will apply to the entire European trade, including European timber producers. The Commission proposes use of a risk-based approach to ensure that efforts are proportionate, and focus on the most likely sources of illegal timber. Taking into account ongoing negotiations in the Council and the European Parliament, we have also included the addition of a prohibition on the placing of illegally harvested timber on the Community market for the first time in this assessment. However, given that we expect the only additional costs emerging from this proposition would be the additional costs of bringing prosecutions on those who have demonstrably traded illegal timber, the order of costs outlined in the scenarios below would not change.

1.10 Adoption of the Proposal will be decided by **co-decision of the European Parliament and the Council**. If the Regulation is adopted, then further implementing measures will be decided by the Commission, under comitology procedures. The Commission has stated that the following principles would be respected in developing implementing measures: the need to avoid putting any unnecessary burden on operators; the balance of costs and benefits to operators covered by the Regulation; the need to respect the necessary flexibility in the application of the implementing measures and the need to facilitate the adaptation of small operators to the requirements laid down in this Regulation.

1.11 The Proposal states specifically that FLEGT-licensed timber products will be considered to have been legally harvested. As a result, such timber will not require any further legality assurance, thus stimulating the market for FLEGT timber, and thereby helping to assure those countries that enter into VPAs that their efforts in implementing the licensing system will not place them at a competitive disadvantage with countries that do not engage in VPAs.

1.12 The proposed Regulation also places a duty on domestic operators within the EU to comply with the due diligence approach, in minimising the risk of illegal sources of timber entering their supply chains.

## **2. Purpose and intended effect**

2.1 This **Consultation** Impact Assessment sets out the possible costs associated with various scenarios which might serve to implement the proposed Due Diligence Regulation. It is

published alongside a public Consultation letter and questions which seek comments and input from stakeholders across industry, NGOs and the public. **The 3 scenarios are not intended as a reflection of the true costs of implementation, but rather offer an illustration of the possible range of costs associated with the Regulation**

2.2 The proposed Regulation is intended to provide a broad framework of guiding principles for the proposed new due diligence system. The proposal aims to change the behaviour of operators by requiring them to develop robust systems to minimise the risk of handling illegal timber. As drafted, the proposed Regulation is not intended to provide comprehensive detail of how individual organisations will comply. Such detail will be contained in a Commission implementing regulation taken forward once the parent regulation is agreed.

2.3 Member States will establish the detail of their individual enforcement and compliance systems when putting the Regulation into effect in their territory.

2.4 As a result of the lack of detail on systems for compliance, and in order to prepare for the discussions on the implementing regulations, the UK has prepared initial impact information for three possible scenarios under the Proposed Regulation, on which we would welcome views (see next section).

### 3. Consultation

3.1 Given the tight timescales associated with the negotiation of new Community legislation, we are seeking initial views on the Proposal in a shortened six week public consultation period in preparation for EU discussions. The intention is to seek broad agreement for the principles contained in the proposed Regulation, with a commitment to continue discussion on the specific details of a new system.

3.2 We welcome views on the amendments that have been tabled and adopted by the European Parliament's Committee on the Environment, Public Health and Food Safety.

### 4. Options

4.1 This Consultation Impact Assessment seeks to identify the likely impact of the proposed DDR on a range of UK stakeholders, including **importers** and **timber producers** within the EU, and **different industry sectors**, including furniture, construction and paper under 3 different scenarios.

4.2 We have also attempted to provide a robust assessment of the impacts on **small and medium size enterprises**, whilst recognising that there is incomplete information on the possible impacts on this sector. We have also included information on positive **benefits outside of the UK**, as this is the primary driver of the proposed legislation (although these benefits are difficult to quantify).

4.3 Three possible scenarios for how a due diligence system might be applied by UK timber importers are set out below. We also welcome views on the potential costs and benefits associated with a possible prohibition on placing illegal timber on the community market for the first time.

- **Scenario 1:** Due diligence systems based on operators' self-declaration, but not third-party audited.
- **Scenario 2:** an elevated version of the current systems used by trade associations such as the UK Timber Trade Federation (TTF), which have responsible purchasing policies<sup>2</sup>, combined with the mode of operation of the UK Central Point of Expertise on Timber (CPET)<sup>3</sup>. This scenario assumes that products originating from low-risk countries use a form of self-declaration. All other countries of origin would require the purchase of third-party verification material. All companies would need to be third-party audited. This scenario lies between the two extremes (Scenarios 1 and 3) and is similar to existing practice for timber importers.
- **Scenario 3:** includes third-party auditing, with verified third-party legal timber as the minimum requirement (whether domestically grown or originating outside the EU).

4.4 We have also undertaken an additional analysis on scenario 2, based on different assumptions on the proportion of the timber industry involved in first placing timber on the EU market.

4.5 Estimates have been made for the additional cost per cubic metre or tonne to the different stakeholders for the first three scenarios, as well as estimated overall industry sector costs. All scenarios assume that the onus of ensuring legality is on the operator which first places timber and timber products on the market.

### **Products in scope**

4.6 A list of timber and timber products which fall into scope of the Proposed Regulation is included as an Annex in the proposed Regulation. However, seating (Code Numbers: 94016100 and 94016900), which includes outdoor furniture, appears to be missing from the Annex, as well as furniture wood components. This impact assessment has included these products as it is assumed that this omission is due to an oversight, and is not deliberate.

4.7 The Regulation currently excludes composite material, but includes packaging material (e.g. wooden pallets or containers) that other (non-timber) goods are shipped in. The US Lacey Act<sup>4</sup>, as amended, explicitly excludes packaging (other than shipments of packaging material) because of the complexity of extracting this material from a shipment and investigating its legality. If the proposed Regulation does intend to cover packaging, this could imply that the importers of *any* products transported in wooden packaging materials would be required to establish due diligence systems. After seeking clarification from the Commission, the UK now

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<sup>2</sup> Responsible purchasing policies provide tools for companies to assess the risk of illegal and unsustainable wood products from non-certified sources entering supply chains with different levels of due diligence required depending on whether the source-country risk level is low or high. Companies must set internal targets to systematically eliminate high-risk products and suppliers. All scheme companies must submit an annual report to an independent auditor for verification and to recommend corrective actions. The TTF's scheme<sup>2</sup> draws mainly on the CPET definitions of 'legal' and 'legal and sustainable' timber.

<sup>3</sup> CPET<sup>3</sup> provides detailed information and advice on how public sector buyers and their suppliers can meet the UK government's timber procurement policy requirements in practice. CPET uses a Reference Board to inform the government of forest stakeholders' opinions and positions on the impacts of its timber procurement policy; to advise and make recommendations on its work; and, where appropriate, to communicate planned CPET activities to stakeholders to get feedback, facilitate consultation and ensure transparency. A similar body is envisaged at an EU level for Scenario 2, with the policies applying to private as well as public sector buyers and suppliers of all specified wood products-although this is not currently envisaged in the draft Regulation.

<sup>4</sup> <http://www.fws.gov/le/pdf/lacey.pdf>

understands that packaging *does not* fall in scope of the Regulation, and thus will not incur any associated additional costs.

4.8 It is anticipated that the sale of standing trees are likely to be brought within the scope of the Regulation, and in such cases, the forest owner would likely be the 'Operator', however the detail of this definition is yet to be resolved.

4.9 A more detailed assessment of costs by wood product sub-sector has been conducted (details at Annex 3).

4.10 The results also highlight the high costs associated with tropical hardwood, due to the difficulty of independent verification of legality associated with these specific products. Costs are also uncertain for paper, despite 75% being composite from waste (and thus excluded from the Regulation). **Most significantly, the assessment also illustrates the complexity of the information and supply chains associated with furniture industry. As well as having the largest number of possible companies in scope of the Regulation, information on the current level of legally verified product is also incomplete.**

4.11 There are also specific difficulties with Chinese-sourced plywood in terms of verifying legality, particularly since the external supply chains can be very complex and the source of the face material is frequently unknown. Consequently the Regulation is anticipated to have higher cost implications for UK businesses importing plywood from China.

## 5. Costs and benefits

### Costs to importers of timber

5.1 The table below summarises the expected costs for importers of timber into the UK under each of the three scenarios<sup>5</sup>. Total volumes are not shown, as the units vary between cubic metres and tonnes depending on the product<sup>6</sup>. **It must also be remembered that the number of companies likely to be affected may be inflated for all scenarios, due to the inability to disaggregate information on companies who first place timber on the Community market.**

*Table 1: Summary of annual costs of applying the three scenarios to imported products\**

(million GBP)	Import value	Scenario 1 added purchase cost p.a.	Scenario 1 added admin cost p.a.	Scenario 2 added purchase cost p.a.	Scenario 2 added admin cost p.a.	Scenario 3 added purchase cost p.a.	Scenario 3 added admin cost p.a.
Imports from within EU	3,617.6	0		0		81.3	
Imports from outside the EU (low risk)	384.3	0		0		8.3	
Imports from outside the EU (high risk)	2,342.2	0		146.6		146.7	
<b>Total (million GBP)</b>	<b>6,344.1</b>	<b>0</b>	<b>11.9</b>	<b>146.6</b>	<b>28.8</b>	<b>236.3</b>	<b>19.6</b>
<b>Total costs as % of import value</b>		<b>&lt;0.1%</b>	<b>&lt;0.1%</b>	<b>2.3%</b>	<b>&lt;0.1%</b>	<b>3.7%</b>	<b>&lt;0.1%</b>

*\*UK sourced wood product figures are not shown as there are no additional purchasing costs required. Administration costs are not included as the total is GBP 17,000; however this figure does not include furniture, flooring, board products or 'other' products, which would result in a higher total cost.*

<sup>5</sup> The additional costs of importing wood under scenarios 2 and 3 were calculated directly from UK import data. The assumptions and methodology underlying this assessment are in Annex 1.

<sup>6</sup> The sources for the figures shown in Table 1 are explained in the methodology annex (Annex 1) below and are broken down by sector. The assumption underlying these costs is that imports from within the EU are assumed to be low risk, although it is worth reiterating that the European Commission will develop criteria for assessing high and low risk, in consultation with Member States as part of the subsequent implementing measures process.

5.2 As an illustration of the potential range of costs within these 3 Scenarios, Table 2 below demonstrates alternative figures based on a sensitivity analysis of the ‘first placer’ assumption underlying Scenario 2. **This clearly illustrates that the original assessment of possible annual administrative costs for this particular Scenario could be up to 68% higher or 48% lower if we alter the level of first placers present in the market.** While we have not conducted such an analysis for the other 2 Scenarios, we can assume that the costs may fall by a similar proportion under a similar relaxation of this particular assumption.

*Table 2.: Scenario 2 sensitivity analysis summary of annual costs and set up costs on imported wood products\**

<i>All figures: million GBP per year</i>	<b>Total Admin or Purchasing Cost</b>	<b>Total Import value</b>	<b>Total costs as % of import value</b>
<b>Scenario 2 added purchasing product cost</b>	146.6	6,344.1	2.3%
<b>Scenario 2 admin cost**</b> (Figure from Table 1 above , plus set up costs)	33.2	6,344.1	<0.01%
<b>Lower level of Due Diligence</b> Scenarios 2.1 and 2.4 admin cost	48.25	6,344.1	0.01%
<b>Medium level of Due Diligence</b> Scenarios 2.2 and 2.5 admin cost	32.4	6,344.1	<0.01%
<b>Higher level of Due Diligence</b> Scenarios 2.3 and 2.6 admin cost	16.2	6,344.1	<0.01%

\* UK sourced wood product figures are not shown as there are no additional purchasing costs required. Administration costs are not included as the total is just GBP 17,00 for UK. These figures do not include flooring or board products which would result in a higher total cost.

\*\* This figure did not include the administrative data for ‘other products’ which is included in scenarios 2.4 to 2.6.

5.3 Administrative costs associated with practices that companies already undertake and would continue to take regardless of the Regulation have not been included in our analysis. This means that the higher the proportion of material already derived from low risk sources, which may be demonstrated by independent legal verification or certification, the lower the costs of introducing the Regulation would be. **Consequently, high risk wood product sub-sectors, where a substantial quantity of products originate from or are manufactured in high risk countries with a low level of certification will require comparatively higher additional costs.**

5.4 Table 1 does not include set-up costs, where companies do not already have the appropriate systems in place. **While no hard data exists on the proportion of companies who are currently using some form of due diligence system, it is recognised that a significant proportion of UK industry could be covered through existing practice, notably existing chain of custody schemes.** These set-up costs are one-off, but will add to the overall cost of implementing the proposed Regulation; and are shown in the product subgroup breakdowns in the Annex 3 to this assessment. The assessed additional costs are shown in Table 3 below.

**Table 3: One-off set-up costs to establish Due Diligence systems for the UK Wood Product Industry**

Scenario 1 added cost (million GBP)	Scenario 2 added cost (million GBP)	Scenario 3 added cost (million GBP)
2.1	4.7	13.6

5.5 An internal assessment made by the European Commission in November 2008<sup>7</sup> estimated that it would cost EUR40 million (GBP35.74 million) for the whole of the EU private sector to apply the proposed Regulation. Our analysis suggests that this estimate is very low, given that the cost for the UK is assessed at GBP11.9 million for Scenario 1, GBP175.4 million for Scenario 2 and GBP255.9 million for Scenario 3 for the UK alone. There are also additional, as yet, unqualified costs associated with the implementation of the requirements. These are detailed in Annex 5.

### **Assessment of additional administration costs**

5.6 The overall administration cost for each scenario is obtained by assessing the administrative costs for companies without any due diligence systems in place and/or which do not source third-party legally verified products. The level of administrative costs will vary according to the quality of existing internal data management, the quantity of products and suppliers, the level of legally verified or certified material purchased and whether remaining products are from low or high risk sources. Further, companies which are not those which **first** place timber or timber products on the Community market will not be required to develop a system under this Regulation. The administrative cost is added to the increased purchasing cost and is calculated as follows<sup>8</sup>:

- **Scenario 1:** Administrative costs: one-off set up costs for those companies with no current due diligence system to change internal systems are estimated at 32.5 hours of managerial/clerical time (reduced by 50% for an SME). Annual costs are assessed at 1 day per month for large companies and 0.5 days per month for SMEs.
- **Scenario 2:** Administrative costs: one-off set up costs for those companies with no current due diligence system to change internal systems are estimated at 70 hours of managerial/clerical time (reduced by 50% for an SME). Annual costs are assessed at 1 day per week for large companies and 2 days per month for SMEs in addition to annual independent audit costs.
- **Scenario 3:** Administrative costs: one-off set up costs for those companies with no current due diligence system to change internal systems are estimated at 100 hours of managerial/clerical time (reduced by 50% for an SME). Annual costs are assessed at 1.5

<sup>7</sup> <http://www.agriculture.gov.ie/forestry/TimberTradersRegulation/CionexplanationNov08.pdf>

<sup>8</sup> Methodology and assumptions for the calculation of the admin costs are at Annex 5

day per month for large companies and 1 day per month for SMEs in addition to annual independent audit costs. Annual costs are reduced in scenario 3 compared to scenario 2 as companies would have chain of custody and would be only purchasing legally verified or certified wood products. Once a chain of custody system has been developed and we can assume that all purchasing consists of only legally verified or certified products, then the day-to-day administration costs fall as the system tracks wood products from source with minimal follow-up or paperwork other than the issued certificates.

5.7 The Scenario 2 due diligence system requires more annual administrative costs for a variety of reasons, including the need to assess whether a product source is low or high risk and the follow-up required to obtain the appropriate documentation from low-risk sources. Due to the increased complexity of Scenario 2 compared to Scenario 3, additional time is needed to prepare the annual report and assessment. Furthermore, many smaller sized companies are unfamiliar with illegal logging issues and these companies may find it difficult to understand how to apply due diligence systems within their purchasing system.

5.8 Scenario 1 would have a comparatively small impact on the UK wood product industry with the relevant costs confined to relatively low administrative costs with no third-party auditing required. Conversely, Scenario 3 would add greater costs to doing business for most product groups and sectors. Scenario 2 would have varying costs depending on the sector and product as many of the larger sized companies across the product sectors have already invested considerable time and expense in obtaining certified and legally verified material.

5.9 In its estimate of the impact of the earlier 'additional options' put forward for consultation by the European Commission, *Indufor* estimated that, regardless of the option selected, the average cost of low-tech legality control systems would remain within a range of 0.22 – 0.34 EUR/m<sup>3</sup> (inclusive of government and private sector costs).<sup>9</sup> These figures are broadly in line with the results of this impact study for Scenario 1. However this impact assessment has found that the cost would be much higher than this for Scenarios 2 and 3 in all cases where data is collected in cubic metres.

### **Costs to operators/producers in the UK**

5.10 UK primary producers of timber products, mainly forest owners who sell wood for financial gain, and secondary producers such as sawmills where these are the same legal entities as primary producers, are expected to fall within scope of the Regulation. They have been included primarily in order to avoid incompatibility with WTO rules on non-discrimination, but also recognising that certain Member States may not have robust systems to ensure legality in place themselves.

5.11 Whilst recognising that the primary source of illegal timber is from third countries outside the EU, the due diligence approach is intended to be compatible with a range of existing criteria and best practice in the EU. **The incidence of illegal logging in the UK is understood to be low, with** illegal felling at less than 1% of private felling operations (which accounts for about 45% of all felling operations at present). Based on the draft Regulation it is unclear exactly how domestic operators will be required to implement due diligence systems. However it is our intention to build upon existing mechanisms and frameworks wherever this is possible, such as

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<sup>9</sup> <http://www.illegal-logging.info/presentations/17-180108/puustjarvi.pdf>

through a felling licence and the requirements of the UK Forestry Standard<sup>10</sup>. As a result, the associated costs from the proposed Regulation to domestic industry are expected to be low. More information on compatibility with existing UK practice is at Annex 5.

5.12 The UK domestic timber industry already has systems for the management of forests and supply chains for timber and assuring compliance with standards; including forest certification systems and legality verification schemes. The draft Regulation seeks to harmonise any new action with existing agreed standards and best practices, whether for importers of timber from third countries, or for producers in the UK.

5.13 Professionally managed and forests managed on an *ad hoc* basis will need to have in place due diligence systems and procedures which demonstrate that applicable legislation is being complied with. This will be provided by a combination of internal systems and, particularly in the case of private forests, the requirements for obtaining a felling licence and or a forest management plan.

5.14 UK Forestry Ministers have made it a major aim to encourage more owners to bring their small woodlands back into management; they recognise that any due diligence systems must be proportionate and not create any unnecessary barrier or disincentive to managing these woodlands.

## **Benefits**

5.15 The benefits of this policy accrue predominantly outside of the UK borders so need to be seen in the context of wider development, environment and climate change policy. A number of studies have estimated the cost of illegal logging to forests nations. The World Bank estimates costs of illegal logging at \$15bn per year reporting that “*where illegal logging in public lands alone causes estimated losses in assets and revenue in excess of US\$10 billion annually*”<sup>11</sup> and that “*As much as US\$5 billion is lost annually to governments because of evaded taxes and royalties on legally sanctioned logging*” (World Bank<sup>12</sup>). Forestry contributes about 10% of GDP in 19 African countries and about 10% of trade in ten African countries. Over two-thirds of all African people rely on forests for their livelihoods (Millennium Ecosystem Assessment).

5.16 Assuming that the UK takes a share of illegal timber relative to its share of the global timber market<sup>13</sup> this would imply that by importing illegal timber, the UK is indirectly responsible for costs of approximately £425bn per year being inflicted upon the governments, economies and societies of tropical forest nations. To place this cost in context, this is equivalent to 11% of DfID’s total expenditure in 2008<sup>14</sup>. If trade in illegal timber were prevented, as opposed to being transferred to other countries without due diligence regimes, there would likely be significant

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<sup>10</sup> The UKFS sets out the approach of the governments in the UK to sustainable forest management (SFM). As the foundation for SFM in the UK, the UKFS sets standards, provides a basis for the Regulation and for domestic monitoring (including national and international reporting); and indicates sources of guidance.

<sup>11</sup> This estimate is based on the global annual value of timber logged illegally on public lands, including the full value in this cost benefit analysis implicitly therefore assumes that there is no net benefit to forest nations of illegal logging, or that the benefits of any revenues are offset by the negative social impacts of illegal activity that are also highlighted in the World Bank report which are not quantified elsewhere.

<sup>12</sup> [http://siteresources.worldbank.org/INTFORESTS/Resources/ForestLawFINAL\\_HI\\_RES\\_9\\_27\\_06\\_FINAL\\_web.pdf](http://siteresources.worldbank.org/INTFORESTS/Resources/ForestLawFINAL_HI_RES_9_27_06_FINAL_web.pdf)

<sup>13</sup> 2005 estimates place the value of the global trade in forest products (including furniture, books etc) at about £150 billion. The equivalent figure for UK imports of forest products was £6.0 billion. An exchange rate of £1=US\$1.41

<sup>14</sup> DfID Annual Report 2008: <http://www.dfid.gov.uk/pubs/files/departmental-report/2008/default.asp>

development benefits. These would accrue because a reduction in illegal logging would help to deliver the wider international development and environment objectives of the UK Government.

5.17 It is important to note that the cost to overseas economies may differ, depending on whether the UK share of trade in illegally logged timber is larger or smaller than its share in the timber trade as a whole. It may also be lower if the due diligence regime is not 100% effective and some illegally harvested timber products do still enter the UK, or alternatively, if illegal logging continues but illegal timber is simply sold into markets outside of the EU. The opposite is also true: if the EU due diligence regime has a significant impact on forest governance and illegal logging is reduced more widely than the scale of imports into the EU, the effects could be greater than estimates based simply on proportional market share. As a very simple measure to provide a range of benefits: a lower bound estimate of 50% of £425bn could be used for the weaker due diligence option.

5.18 There are also likely to be wider environmental benefits of reduced illegal logging. The Eliasch Review<sup>15</sup> estimated that in five out of ten of the countries with the largest forest cover in the world, more than half of the trees cut were illegally felled. Poor Regulation and law enforcement are widely recognised as important underlying drivers of deforestation. With the forestry sector accounting for roughly 17% of global greenhouse gas emissions (making it the third largest source of emissions) it is clear that improved governance will be key to help tackle this huge source of emissions.

5.19 Beyond carbon, forests provide a wide range of social and environmental services, for example: water conservation and purification, rainfall generation, soil protection and conservation and the supply of food, fuel and medicinal resources, as well as the protection of globally important wildlife habitats. Forests also harbour globally important biodiversity reserves. In addition to carbon storage, the value of these services is not included within the financial benefits (and associated costs accruing from the loss of those services), as highlighted above. A recent report on the costs of policy inaction for the global Economics of Ecosystems and Biodiversity Study (TEEB), led by a Deutsche bank economist Pavan Sukhdev, estimated that the cost of the loss of these services for one year's worth of deforestation at between \$2 trillion and \$5 trillion<sup>16</sup>.

5.20 Whilst difficult to quantify it is clear that reducing illegal logging will have direct economic benefits to forest nations, supporting UK international development goals, and that there will also be significant environmental and social benefits if deforestation is also reduced as a result. Beyond this, improving forest governance will also help the long term aim of reducing greenhouse gas emissions from the forest sector. Controlling and reducing the trade in illegally harvested timber will support climate change mitigation, and greenhouse gas reduction targets as well.

5.21 Benefits have been presented in the same range for each option as it is assumed that a policy would not be implemented that could not deliver a reduction in illegal logging.

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<sup>15</sup> [http://www.occ.gov.uk/activities/eliasch/Full\\_report\\_eliasch\\_review\(1\).pdf](http://www.occ.gov.uk/activities/eliasch/Full_report_eliasch_review(1).pdf), page 58

<sup>16</sup> [http://ec.europa.eu/environment/nature/biodiversity/economics/teeb\\_en.htm](http://ec.europa.eu/environment/nature/biodiversity/economics/teeb_en.htm)

## 6. Small Firms' Impact Test

6.1 There is a lack of solid information about the nature of SME involvement in the UK timber market, and the proportion of operators with existing due diligence systems in place. We are working with the elements of the Small Firms Impact Test devised by the Department for Business Enterprise and Regulatory Reform to build our evidence base, but would specifically welcome further information from consultees on the possible impacts of the Proposal.

6.2 The current proposed Regulation does *not* include any exemptions for minimum amounts of timber or timber products placed on the Community market. The consequences of the provision can be assumed to exempt certain businesses from the requirement of due diligence, and therefore result in a reduction of costs to those businesses. The nature and extent of any such costs have not yet been quantified. We would welcome further information from consultees on the expected costs to SMEs and others to accrue from compliance with the Commission's Proposed Regulation, and the amendments adopted by the European Parliament's Committee on the Environment, Public Health and Food Safety.

6.3 Our initial assessment has concluded that:

- As a result of the existing pattern of market demand for verified legal and sustainable wood products, there is a larger proportion of large companies than small and medium-sized enterprises (SMEs) that have due diligence practices or chain of custody systems in place. For this reason, it is anticipated that the proposed Regulation will have comparatively high cost implications for SMEs for all scenarios.
- There has been a rising trend in recent years of increasing imports of pre-assembled joinery products. This process has been driven by various factors, including a joinery skills shortage and a desire to raise quality standards and to simplify the on-site construction process. There is a strong divide between the large Builders, Joinery and Carpentry companies, some of which have achieved nearly 100% purchasing of legally verified products, and SMEs, very few of which have due diligence or chain of custody processes in place. However the smallest companies tend to deal with only landed stock and purchase their products from timber suppliers, thus not importing directly.

## 7. Competition Assessment

7.1 The Draft Proposal aims to take advantage of existing good practice in the UK market, both in terms of UK timber producers, but also UK timber importers. The Regulation aims to raise the bar to incentivise change in the industry, through sharing of good practice systems.

7.2 The UK is in a good position to benefit from the proposed Regulations, as UK industry is recognised as already containing a body of expertise on chain of custody systems and legality verification, and is thus well placed to compete in any new environment.

7.3 There are likely to be some costs which we have not yet quantified for UK industry if other EU Member States do not fully implement the Regulation. For example, weaker enforcement and penalties regimes in some EU Member States could lead businesses to import their timber through such countries. However, we do envisage that potential additional transport and storage costs associated with a change of import route would significantly influence decisions on altering supply chains to route timber through alternative EU ports.

## **8. Enforcement, sanctions and monitoring**

### **Enforcement and Sanctions**

8.1 In accordance with the allocations of competence between the European Commission and Member States, the Proposed Regulation does not include specific provision for any matter of enforcement beyond the need for effective, proportionate and dissuasive penalties, which are to be determined at Member State level. Costs associated with the new enforcement regime, for ensuring both the appropriate implementation of due diligence systems, as well as for any prohibition, will be considered as an integral part of the process of putting into place domestic legislation giving effect to the Regulation, including for example, introducing relevant offences and corresponding penalties.

8.2 We will endeavour to ensure that the UK enforcement regime is complementary to the systems already in place, and will seek to avoid duplication of inspection and enforcement efforts, in line with Hampton principles.

### **Compliance Monitoring**

8.3 The Regulation proposes a system for monitoring of compliance with the Regulation by Competent Authorities (CA) in Member States. The Competent Authority's duties would include checking that operators are implementing due diligence systems and approval and monitoring of the proposed 'Monitoring Organisations'. The Regulation does not stipulate how operators, or Monitoring Organisations themselves, should be monitored. Further details will be contained in Commission implementing regulations or developed as part of the UK's domestic legislation giving effect to the Regulation. Related costs have therefore not yet been quantified.

### **'Monitoring Organisations'**

8.4 The Regulation contains provision for Monitoring Organisations (MO) which, upon meeting a set of criteria, would be recognised by Competent Authorities. MOs would develop due diligence systems that would be available for operators to use, and must ensure effective implementation by those operators. Whilst operators are not obliged to use MOs, they may find their services a useful means to ensure their compliance with the Regulation. This is especially likely to be the case for SMEs who would thereby avoid the need to develop their own due diligence systems, although the use of the due diligence system of a Monitoring Organisation would be charged for.

## **9. Implementation and Delivery plan**

9.1 Once agreement has been reached on the Proposed Regulation, further processes will follow to agree implementing regulations for the new regime at the EU level, and then to bring the Regulation and the associated implementing regulations into effect in the UK. As a result, timelines are unclear. The UK will work to ensure sufficient lead in time for entry into force of the new requirements in the UK to allow for industry and competent authorities to make adjustments to systems.

## **10. Post Implementation Review**

10.1 The UK will seek the introduction of a review clause into the Regulation.

## Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

**Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.**

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Y	N
Small Firms Impact Test	Y	N
Legal Aid	N	N
Sustainable Development	Y	N
Carbon Assessment	Y	N
Other Environment	Y	N
Health Impact Assessment	N	N
Race Equality	N	N
Disability Equality	N	N
Gender Equality	N	N
Human Rights	Y	N
Rural Proofing	N	N

## Annex 1: Methodology for costing each import scenario

### *Assessment of additional import costs*

The additional costs of importing timber and timber products under scenarios 2 and 3 were calculated directly from UK import data provided by the Forestry Commission. The following assumptions are made, based on discussions with importers and industry experts:

- Likely price premiums required for sourcing independently verified wood products from a particular country rise as the proportion of forest land that is already certified or has been assessed against legality standards falls. As far as possible the data for certified forest area is given separately for softwoods and hardwoods, as in some countries (e.g. the US and Brazil), the situation with regard to certification of each wood type is very different. In the US, for example, while over 50% of softwood forest area is certified, less than 10% of hardwood forest area is certified.
- Likely price premiums will rise up to 8% in those countries with less than 10% of forest land that is already certified or legally verified. While studies have shown that price premiums for legally verified wood in the current market rarely exceed 4%, it is believed that just about all legally verified products placed on the market to date have derived from large centrally managed concession areas. Furthermore, existing legally verified products all tend to be relatively simple (comprising logs and sawn lumber rather than further processed and composite products). The existing price premiums apply to conditions of relatively limited demand for legally verified wood products. Consequently, it is believed that more significant price premiums would be demanded in circumstances where the new due diligence requirements create stronger demand for legally verified wood and where these requirements also have to be imposed on more complex supply chains (e.g. where wood is sourced from numerous small private forest owners) and more complicated products.
- Under scenario 3, price premiums are applied to all sources of supply, both low and high risk. Under scenario 2, price premiums are applied only to high risk countries. It is assumed that the costs of providing confirmation of low risk of illegal logging under scenario 2 would be negligible. This is based on the practical experience of the American Hardwood Export Council, which commissioned an independent peer-reviewed study which demonstrated that there is a less than a 1% chance of any US hardwood being derived from an illegal source. It is assumed that this assurance would be sufficient to demonstrate conformance of all American hardwoods to the scenario 2 legislation without the need for any further action by US exporters. Given that the study has been developed to satisfy requirements for green procurement policy throughout the EU and Japan, which together consume a total of around 800,000 m<sup>3</sup> of American hardwood sawn lumber each year, and that the study has an anticipated shelf-life of five years before being repeated, the costs to American hardwood producers of providing this assurance amounts to no more than around 3 cents per m<sup>3</sup> per year. Under Scenario 2 it is assumed that other low-risk suppliers could commission similar studies at equivalent cost to provide this level of assurance that wood is legal.

## **Annex 2: Other costs which remain difficult to quantify**

### ***Transaction costs at point of import into the EU***

The Regulation does not involve any controls at the Community border so it is unlikely that any extra administration costs will be incurred that might cause undue delays as part of any enforcement or compliance checks.

### ***Trade Diversion***

There is the potential for trade diversion away from the UK into other EU countries if legislation is not applied equally within the EU. This point was made strongly by the trade associations and companies interviewed for the impact assessment. Provided that there are no differences in the application of the Regulation throughout the EU, then limited trade diversion is anticipated.

If the Regulation is unevenly applied, however, with specific countries seen as 'soft', then it is quite possible that timber and timber products from high risk countries will arrive in UK via other EU countries (with a caveat that this is mitigated somewhat through associated increased transport costs), with two key implications:

- An impact on UK agents and importers as UK customers may seek to purchase cheaper products (due to a lack of due diligence) elsewhere in the EU.
- UK exports may also be affected by trade diversion through other EU ports, because there is a risk that countries with less robust enforcement of the proposed legislation will carry out value added manufacturing at a reduced cost, thereby providing competition to UK companies.

Tropical hardwood products and manufactured products will probably be affected most by these eventualities.

Suppliers in high risk countries may also prefer to sell to customers in EU countries which enforce the proposed Regulation least strictly. This would mean that UK traders may find it more difficult (and costly) than those in other countries to source wood products from high risk countries.

## Annex 3: Breakdown of Impact Assessment by wood product sub-sector

### Softwood logs, Sawn wood and Veneer

**Table 3: Annual costs plus set up costs for Softwood logs, Sawn wood and Veneer**

(000 GBP)		Scenario 1 added cost	Scenario 2 added cost	Scenario 3 added cost
<b>Large companies administration</b>	Annual admin rate (importers)	9	25	25
	Set-up cost (importers)	25	54	165
	Annual admin rate (UK only)	n/a	0	0
	Set-up cost (UK only)	n/a	0	0
<b>SME administration</b>	Annual admin rate (importers)	80	360	238
	Set-up cost (importers)	46	108	277
	Annual admin rate (UK only)	n/a	0	38
	Set-up cost (UK only)	n/a	0	59
<b>Softwood logs</b>	High risk	n/a	398	398
	Low risk	n/a	0	27
	EU	n/a	0	351
<b>Softwood Sawn wood</b>	High risk	n/a	10,338	10,338
	Low risk	n/a	0	537
	EU	n/a	0	11,265
<b>Softwood veneer</b>	High risk	n/a	106	106
	Low risk	n/a	0	43.00
	EU	n/a	0	173.00
<b>UK softwood Sawn wood</b>	UK	n/a	0	0
<b>Total additional scenario cost (GBP)</b>		<b>126</b>	<b>865</b>	<b>1,916</b>
<b>Cost per 000 m<sup>3</sup></b>		<b>0</b>	<b>1</b>	<b>5</b>

The TTF and CONFOR commissioned study shows that 58% of imported softwood Sawn wood was certified.<sup>17</sup> Additional studies commissioned by TTF show that this percentage was set to increase and is likely to be much higher in 2008.<sup>18</sup> The high levels of certified materials available in this sector have resulted in no price premiums available for most products. Fewer costs are associated in this sector than for the hardwood sector under scenarios 1 and 2. Higher costs are expected under scenario 3 as the majority of softwood products, for which certification is more straightforward, are already certified, leaving the Regulation to bite upon those remaining products for which certification is less straightforward to achieve.

<sup>17</sup> [http://www.illegal-logging.info/uploads/Timber\\_Importing\\_Trading\\_Sector.pdf](http://www.illegal-logging.info/uploads/Timber_Importing_Trading_Sector.pdf)

<sup>18</sup> [http://www.illegal-logging.info/item\\_single.php?item=document&item\\_id=177&approach\\_id=](http://www.illegal-logging.info/item_single.php?item=document&item_id=177&approach_id=)

## Hardwood logs, Sawn wood and veneer

**Table 4: Annual costs plus set up costs for hardwood logs, Sawn wood and veneer**

(000 GBP)		Scen- ario 1 added cost	Scen- ario 2 added cost	Scen- ario 3 added cost
<b>Large companies administration</b>	Annual admin rate (importers)	37	98	98
	Set-up cost (importers)	11	25	64
	Annual admin rate (UK only)	n/a	0	5
	Set-up cost (UK only)	n/a	0	7
<b>SME administration</b>	Annual admin rate (importers)	92	415	275
	Set-up cost (importers)	29	62	190
	Annual admin rate (UK only)	n/a	0	14
	Set-up cost (UK only)	n/a	0	21
<b>Hardwood logs</b>	High risk	n/a	1,006	1,006
	Low risk	n/a	0	1,788
	EU	n/a	0	831
<b>Hardwood Sawn wood</b>	High risk	n/a	1,381	1,381
	Low risk	n/a	0	4,352
	EU	n/a	0	3,460
<b>Hardwood veneer</b>	High risk	n/a	423	423
	Low risk	n/a	0	3,058
	EU	n/a	0	693
<b>Other hardwood*</b>	High risk	n/a	14	14
	Low risk	n/a	0	27
	EU	n/a	0	66
<b>UK hardwood Sawn wood</b>	UK	n/a	0	0
<b>Total additional scenario cost</b>		<b>169</b>	<b>3,424</b>	<b>17,772</b>
<b>Cost per 000 m<sup>3</sup> (GBP)</b>		<b>0.18</b>	<b>4</b>	<b>19</b>
<b>Cost per tonne (other hardwood*) (GBP)</b>		<b>0.19</b>	<b>4</b>	<b>20</b>

*\*There is a range of products – primarily planed, sanded, finger jointed Sawn wood – where the data is available in tonnes rather than cubic metres.*

For hardwood products, there are substantial differences between tropical and temperate imports because tropical hardwood products have a much lower level of certification and temperate hardwood tends to come from lower risk countries. The 2005 research by TTF and CONFOR shows a comparatively low level of hardwood Sawn wood that is certified (10.5%). Whilst this is expected to have increased since the research was undertaken, the level of certification is still low compared to softwood.

Tropical hardwood logs, Sawn wood and Veneers are the only sectors that currently appear to be actively seeking legally verified material due to the difficulty in obtaining certified products and the mainly high-risk countries they are sourced from. Further, partly as a result of this demand, the levels of legally verified and certified material are expected to have increased considerably since 2005. In somewhat of a contrast, specialist tropical hardwood importers often consider that reaching a purchased volume of 40–50% legally verified product would be a high level of verification. An average percentage is assessed at around 30% of purchases for larger companies.

Flooring figures are provided under the BJC (building, joinery and carpentry) sub-sector but the administrative costs are anticipated to be similar to those identified in the sawn wood and veneer sub-sectors. Recent research: ***Buyer Beware – An Investigation into Merbau Wood Flooring Sales in the UK*** (EIA report, October 2008)<sup>19</sup>, demonstrates that there is a substantial amount of potentially illegal product in the tropical / luxury flooring sector.

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<sup>19</sup> <http://www.illegal-logging.info/uploads/BuyerBeware.pdf>

## Plywood and board products

**Table 5: Annual costs plus set up costs for Plywood, Particleboard and Board products**

(000 GBP)		Scenario 1 added cost	Scenario 2 added cost	Scenario 3 added cost
Administration: not included due to the risk of double-counting, as the majority of companies already have these costs accounted for through existing certification or with other hard and softwood Sawn wood or veneer products.				
<b>Particleboard</b>	High risk	n/a	30	30
	Low risk	n/a	0	327
	EU	n/a	0	6,661
<b>Fibreboard</b>	High risk	n/a	7	7
	Low risk	n/a	0	41
	EU	n/a	0	310
<b>Softwood plywood</b>	High risk	n/a	5,760	5,760
	Low risk	n/a	0	64
	EU	n/a	0	695
<b>Hardwood plywood</b>	High risk	n/a	9,789	9,789
	Low risk	n/a	0	39.00
	EU	n/a	0	642.00
<b>UK sourced wood based panels</b>	UK	n/a	0	0
	<b>Total additional scenario cost</b>	<b>0</b>	<b>15,586</b>	<b>24,365</b>
	<b>Cost per 000 m<sup>3</sup> (GBP)</b>	<b>0</b>	<b>1</b>	<b>2</b>

Particleboard and fibreboard have high levels of certification (60.5% in 2005), particularly with more PEFC products coming online, and relatively low costs per unit reflect this, as well as the absence of any additional administrative costs. The main issues in this sub-sector are for hardwood plywood as higher costs may be incurred due to the difficulty in tracing back to source where tropical material is used. In addition, where different core and face wood products are used in plywood, it is often more difficult (and more expensive) to implement a chain of custody system.

There are specific difficulties with Chinese-sourced plywood in terms of verifying legality, particularly since the external supply chains can be very complex and the source of the face material is frequently unknown. Consequently the Regulation is anticipated to have higher cost implications for UK businesses importing plywood from China.

## BJC Products

**Table 6: Annual costs plus set up costs Builders, Joinery and Carpentry (BJC) products**

(000 GBP)		Scenario 1 added cost	Scenario 2 added cost	Scenario 3 added cost
<b>Large companies administration</b>	Annual admin rate (importers)	231	614	613
	Set-up cost (importers)	66	155	400
	Annual admin rate (UK only)	n/a	0	5
	Set-up cost (UK only)	n/a	0	7
<b>SME administration</b>	Annual admin rate (importers)	512	2,296	1,522
	Set-up cost (importers)	162	459	884
	Annual admin rate (UK only)	n/a	0	14
	Set-up cost (UK only)	n/a	0	21
<b>BJC</b>	High risk	n/a	15,246	15,246
	Low risk	n/a	0	2,590
	EU	n/a	0	8,490
<b>UK sourced BJC</b>	UK	n/a	0	0
<b>Total additional scenario cost</b>		<b>971</b>	<b>18,770</b>	<b>29,791</b>
<b>Cost per tonne (GBP)</b>		<b>0</b>	<b>4</b>	<b>6</b>

Approximately 330,000 people are employed in the BJC manufacturing sector with sales of £6 billion. Total UK sales of woodwork and joinery were £3,934 million<sup>20</sup> in value in 2007. Interviews for the impact assessment revealed that a marked feature of the BJC sector is the majority of SME businesses, many of which employ less than 10 people (possibly 80% of the sector).

<sup>20</sup> [http://www.statistics.gov.uk/downloads/theme\\_commerce/PRA-20070/PRA20300\\_20070.pdf](http://www.statistics.gov.uk/downloads/theme_commerce/PRA-20070/PRA20300_20070.pdf)

## Flooring

**Table 7: Annual costs for Flooring products**

(000 GBP)		Scenario 1 added cost	Scenario 2 added cost	Scenario 3 added cost
Administration: Insufficient discrete data on flooring to be able to make an assessment of costs. See also softwood and hardwood Sawn wood and veneer for related administration costs.				
<b>Flooring</b>	High risk	n/a	1,381	1,381
	Low risk	n/a	0	4,352
	EU	n/a	0	3,460
<b>UK sourced flooring</b>	UK	n/a	0	0
	<b>Total additional scenario cost (GBP)</b>	<b>0</b>	<b>1,381</b>	<b>9,193</b>
	<b>Flooring cost per tonne</b>	<b>0</b>	<b>0</b>	<b>0</b>

Flooring is included in BJC, but see also the Hardwood logs, Sawn wood and Veneer sections for additional information, as many importers deal in flooring in addition to other softwood and hardwood products. For this reason, the addition of administrative costs in this section is likely to introduce double-counting.

## Wooden Furniture

**Table 8: Annual costs plus set-up costs for Wooden Furniture**

(000 GBP)		Scenario 1 added cost	Scenario 2 added cost	Scenario 3 added cost
<b>Large companies administration</b>	Annual admin rate (importers)	154	409	408
	Set-up cost (importers)	44	104	266
	Annual admin rate (UK only)	insufficient data		
	Set-up cost (UK only)	insufficient data		
<b>SME administration</b>	Annual admin rate (importers)	5,394	24,210	16,042
	Set-up cost (importers)	1,706	3,626	11,073
	Annual admin rate (UK only)	insufficient data		
	Set-up cost (UK only)	insufficient data		
<b>Furniture</b>	High risk	n/a	61563	61563
	Low risk	n/a	0	1788
	EU	n/a	0	491983
<b>Wooden seats</b>	High risk	n/a	39,034	39,034
	Low risk	n/a	0	808
	EU	n/a	0	20,296
<b>Wood furniture components</b>	High risk	n/a	203,329	203,329
	Low risk	n/a	0	5,336
	EU	n/a	0	104,363
UK Soft/ Sawn wood	UK sourced	n/a	0	0
<b>Total additional scenario cost (GBP)</b>		<b>7,099</b>	<b>89,399</b>	<b>582,450</b>
<b>Cost per tonne (GBP)</b>		<b>2</b>	<b>21</b>	<b>139</b>

There are approximately 75,000 companies involved in the furniture industry with estimates of upwards of 7,000 companies involved in manufacturing. Contract furniture (i.e. office furniture) has a much higher level of PEFC and FSC certification than other furniture segments. This is due to high customer demand in this segment including central government (OGC) procurement policies as well as social housing. It is considered essential for this market to have high environment credentials. Industry interviewees suggested that certification for furniture across the kitchen and office sectors could be as high as 75%.

The main issues in the furniture sector are for veneers from tropical hardwood and hardwood plywood-based products. As is common across all sectors, it is generally the larger companies that have more due diligence policies in place and are actively seeking certified products.

Wooden seating, shop furniture and other wooden components is not included in the proposed Regulation as it stands. (Upholstered furniture is not included here, or in the proposed legislation.) Garden furniture has long been a contentious issue and large retailers have actively focused on sourcing certified products in recent years. This is exemplified by the 73 chain of custody certificates specifically for garden furniture currently listed by FSC (the PEFC database does not break down their information to product level).

## Other products

**Table 9: Annual costs plus set up costs for 'other' wood products**

<b>Fuel wood, charcoal, frames, boxes and barrels</b>				
		<b>Scenario 1 added cost (000 GBP)</b>	<b>Scenario 2 added cost (000 GBP)</b>	<b>Scenario 3 added cost (000 GBP)</b>
Administration: Insufficient discrete data to be able to make an assessment of costs.				
<b>Wood products (other)</b>	High risk	n/a	3,172	3,172
	Low risk	n/a	0	2,590
	EU	n/a	0	1,527
<b>UK sourced wood products (other)</b>	UK	n/a	0	0
	<b>Total additional scenario cost (GBP)</b>	<b>0</b>	<b>3,172</b>	<b>7,289</b>
	<b>Cost per tonne (GBP)</b>	<b>0</b>	<b>10</b>	<b>24</b>

Information is more difficult to ascertain for these groups than for other sectors and it is unknown how many companies are operating in these sectors. We would welcome any information on these sectors that consultees might be able to provide.

## Pulp and paper

**Table 10: Annual costs plus set up costs for pulp and paper products**

(000 GBP)		Scenario 1 added cost	Scenario 2 added cost	Scenario 3 added cost
<b>Large companies administration</b>	Annual admin rate (importers)	15	41	41
	Set up cost (importers)	4	10	27
	Annual admin rate (UK only)	0	0	0
	Set up cost (UK only)	0	0	0
<b>SME administration</b>	Annual admin rate (importers)	77	346	229
	Set up cost (importers)	24	52	158
	Annual admin rate (UK only)	0	0	0
	Set up cost (UK only)	0	0	0
<b>Pulp and paper</b>	High risk	n/a	18286	18286
	Low risk	n/a	0	19948
	EU	n/a	0	102281
<b>Total additional scenario cost</b>		<b>121</b>	<b>18,735</b>	<b>140,970</b>
<b>Cost per 000 tonne (GBP)</b>		<b>0</b>	<b>0</b>	<b>0</b>

More than 12 million tonnes of paper is utilised in UK, with 7 million tonnes imported via paper agents and merchants. Around 75% of UK paper production uses recovered waste paper which is not included in this Regulation.

Compared to timber imports there is less specific data available on the levels of certification and legal verification. Industry insiders claim a very high level of certification, with all the large mills having chain of custody systems in place. External observers, including WWF, claim that a higher level of illegally sourced paper and pulp products enters the country than is widely understood within the Industry. Consolidating the information we have available, it appears that for some products (e.g. for printing and writing papers) there is a high level of certification. However, the speciality papers, particularly those from the smaller 100 plus suppliers, appear to have a much lower level of legal verification.

A recent WWF study published in July 2008 provides further insight into the paper sector, particularly for paper sourced from Indonesia.<sup>21</sup>

<sup>21</sup> <http://www.illegal-logging.info/uploads/WWFEUimports.pdf>

## Annex 4: Domestic Timber Producers

### Background to UK Forestry

The UK defines domestic sustainable forest management through the UK Forestry Standard and the current definition is 'the stewardship and use of forests and forest lands in a way, and at a rate, that maintains their biodiversity, productivity, regeneration capacity, vitality and their potential to fulfil, now and in the future, relevant ecological, economic and social functions, at local, national and global levels, and that does not cause damage to other ecosystems' (Second Ministerial Conference on the Protection of Forests in Europe; Helsinki, 1993).

It is important to put the UK forest industry in context compared to other countries. The vast majority of timber produced in the UK comes from legal sources. The UK is the 4th largest net importer of forest products (behind USA, China & Japan). However, this does not make us the 4th largest importer overall (Germany imports more than us, but also has much a higher level of exports). Much of the primary timber products being imported into the UK from EU-27 and Non-EU-27 sources are certified or come with other documentation to demonstrate legality and sustainability criteria. A successful risk assessment procedure would require that the level of detail for an assessment, and the associated mitigation steps which are required to be taken, are proportionate to the risk. The requirement for a comprehensive risk assessment to establish legality as part of a due diligence system is only needed for relatively small volumes of timber within the UK.

The following tables provide detail on the scale of UK production and imports onto the UK. The tables below show that the volume of primary timber products being imported from countries other than EU-27 sources is c 3.6 million cubic metres during 2007. The UK imports of primary timber products from outside of the EU represent around 5% of all such imports into the EU.

**Table 11: UK production and imports, 2007**

	Production	Imports	% Imported
		000 m <sup>3</sup>	
Roundwood	9,018	464	5%
Sawn wood	3,146	8,402	73%
Woodbased panels	3,549	3,891	52%
Veneer sheets	0	33	100%
Plywood	0	1,624	100%
Particleboard	2,684	1,196	31%
Fibreboard	865	1,038	55%
Total primary wood products	15,713	12,758	45%

Source: Forestry Commission (JFSQ 2008 return to international organisations, compiled from various sources).

Notes:

1. Data on production of secondary wood products not available.

**Table 12: Source of imports to the UK, 2007**

	EU-27	China	Tropical countries	Other countries	<b>Imports from Countries other than EU-27 (thousand m3)</b>	Total imports (thousand m3)
Roundwood	82%	0%	2%	16%	<b>85</b>	464
Sawn wood	75%	0%	3%	23%	<b>2,126</b>	8,402
Woodbased panels	65%	11%	16%	7%	<b>1,355</b>	3,891
Veneer sheets	75%	5%	4%	17%	<b>8</b>	33
Plywood	18%	28%	41%	13%	<b>1,331</b>	1,624
Particleboard	96%	0%	0%	4%	<b>51</b>	1,196
Fibreboard	94%	1%	2%	3%	<b>66</b>	1,038
<b>Total primary wood products</b>	<b>72%</b>	<b>4%</b>	<b>7%</b>	<b>17%</b>	<b>3,555</b>	<b>12,758</b>

Source: HM Revenue & Customs

Notes:

1. Data on imports of secondary wood products currently shown as metric tonnes (thousands).
2. Numbers have been independently rounded

## Annex 5: Methodology and assumptions underlying admin cost calculations

Daily costs have been assessed using UK government (BERR) data intended for impact assessments. A variety of data sources have been used to compile the impact assessment, including official trade statistics, trade associations, FSC<sup>22</sup> and PEFC<sup>23</sup> data and prior research carried out privately or by NGOs as well as information garnered by telephone interviews.

It is difficult to ascertain the number of companies that have due diligence processes in place, particularly further down the supply chain, as there is no official or trade body that currently collects this information. Detailed information is available for logs, Sawn wood, veneer and board products as the percentages of product legal verification and certification (but not number of companies) are regularly researched by TTF and CONFOR trade associations. The existing levels of known (or estimated) certified material available have been used as a guide to assess the number of UK companies using a due diligence approach.

There is detailed information available at the UK primary processing level but there is comparatively little disaggregated data available to show the level of manufactured products which solely originate from UK forests such as in furniture and BJC (Builders, Joinery and Carpentry) sectors. UK forestry products are considered to be low risk with the costs involved below that of sourcing from outside the EU due to simpler supply chains and the knowledge of the group certification schemes in operation in the UK, which reduce the auditing costs to around £500 per annum.<sup>24</sup>

Whilst the number of companies involved in the sub-sectors is available from the Office of National Statistics<sup>25</sup> and the Forestry Commission<sup>26</sup> the data is not available to distinguish between the first operators that put products on the market in the UK (who will be directly impacted by the proposed Regulation) and those operators that have subsequently purchased these products or subsequently added value. A longer and more detailed study would be required to increase the accuracy of the assessment; therefore the administrative costs outlined in this impact assessment should be considered as indicative rather than actual costs.

This Impact Assessment assumes that a proportion of companies have due diligence systems in place. The proportion was estimated for each sector separately by using information from the number chain of custody certificates issued, the level of certified product (at the point the material was placed on the market for the first time) as well as through interviews with and data from the appropriate trade associations together with government statistical data to assess the numbers of companies involved at the first point in the market. These proportions were differentiated between large and SME companies.

Subsequently, costs for some sectors and company sizes are estimated to be comparatively low (i.e. large companies in the softwood logs, Sawn wood and veneer category) and others much higher (i.e. furniture). The less processed the product, the more reliable the data is, with

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<sup>22</sup> <http://www.fsc-uk.org/product-search/>

<sup>23</sup> <http://register.pefc.cz/search1.asp>

<sup>24</sup> Audit costs vary depending on the auditor selected and the size of company. The impact assessment assumes that group chain of custody schemes would be used as these are an appropriate and cost effective option for the smaller forest product companies that remain uncertified in the UK.

<sup>25</sup> <http://www.statistics.gov.uk>

<sup>26</sup> <http://www.forestry.gov.uk/website/forstats2008.nsf/LUContentsTop?openview&RestrictToCategory=1>

paper and furniture being the most difficult sectors to assess. The **figures below are indicative only, and based on discussions, through site visits.**

The n/a is used where there was insufficient data to make an assessment e.g. casks, and also to reduce the risk of inflating numbers through double counting which might arise as a result of companies importing more than one product type.

Companies with chain of custody or existing due diligence systems are assumed not to have any further administrative costs (the additional import product cost is already accounted for).

**Table 13: Number of UK procuring and importing companies that would need to implement a due diligence system**

Sector	Number of SMEs	Number of larger companies
Softwood Logs, Sawn wood and Veneer	85	3
Hardwood Logs, Sawn wood and Veneer	72	16
Plywood, particleboard and fibreboard	n/a	n/a
Builders Joinery and Carpentry (BJC)	344	79
Flooring	n/a	n/a
'Other' products incl. casks & barrels	n/a	n/a
Wooden furniture	3550	50
Paper	50	5
<b>Total</b>	<b>4101</b>	<b>153</b>

One further cost that is not included is related to the need for operators to update software systems. This is because this is not, strictly speaking, an essential requirement. Although I.T. is often seen as essential precursor for implementing a due diligence system, whether it will be required in practice will depend on the size of the company, the range of products imported and the capability of existing I.T.

There will be a large variation in administrative requirements in terms of time, and therefore an estimated average (mean) was used. This time requirement is not a top end figure, particular for the first years of operating a due diligence system.

### **Membership costs associated with using Due Diligence systems developed by trade bodies**

The hugely differing membership costs of the various trade associations (and organisations such as GFTN), that could serve as Monitoring Organisations makes it difficult to assess costs particularly since they are normally tiered according to the company turnover in the previous year. Also, many trade associations also consider this information as confidential to their organisation.

Annual membership fees can range from a few hundred, to tens of thousands of pounds. Generally speaking, the bigger and the more services a trade association provides, the more

expensive its membership fee. Currently, trade bodies might charge separate fees for membership and for their due diligence system. Some organisations have published their current fees for due diligence-type systems on-line at:

[http://public.ftn.wwf.org.uk/filelibrary/pdf/wwf\\_uk\\_ftn\\_membership\\_fees.pdf](http://public.ftn.wwf.org.uk/filelibrary/pdf/wwf_uk_ftn_membership_fees.pdf)

It is unknown at present how many trade associations would want to develop new due diligence systems, improve their existing systems, join forces or make an arrangement with trade associations that have systems already in place - consequently it is unclear how many companies might choose to join an additional membership organisation. It is also worth noting that a number of companies would probably develop their own due diligence systems for use. Views from consultees on these points would be welcomed.

## Annex 6: Additional evaluation of costs in Scenario 2, based on different assumption of the proportion of operators involved in first placing timber on the Community market.

There is insufficient reliable data on the breakdown on the UK wood product supply chain to provide a robust analysis capturing how many companies are ‘first placers’, size of company, number of companies with due diligence processes and whether they source from UK, within EU or outside the EU. Given the urgent requirement to provide an analysis coupled with insufficient time to conduct a full survey; further administrative cost analysis is provided in this paper based on ‘Scenario 2’ as this was seen as the most likely scenario. Using a different formula to calculate the levels of due diligence, a comparison can be made with the main paper which derived the proportion of companies requiring due diligence primarily from industry sources as no hard statistics are available.

**We would particularly welcome further information from stakeholders on the number of companies involved in first placing timber on the community market, and on the proportion of these companies who already have due diligence systems in place.**

There are six sub-scenarios are based on an assessment of the number of companies that are importing wood products and that are also ‘first placers’ of product onto the market. The sub-scenarios are as follows:

- A: The first group of sub-scenarios are at a due diligence level of 70% (scenario 2.1), 80% (scenario 2.2) and 90% (scenario 2.3) for products measured in square or cubic meters. This group of products has a lower level of manufacturing with a comparatively high level of certification.
- B: The second group of sub-scenarios are at a due diligence level of 25% (scenario 2.4), 50% (scenario 2.5) and 75% (scenario 2.6) for products measured in tonnes. This group of products has a higher level of manufacturing with a comparatively low level of certification. Furniture is a much disaggregated sector with little documentation on due diligence levels and this further analysis provides a more detailed breakdown to be made.

*Table 1: Summary of annual costs of applying the Scenario 2 to imported wood products\**

<b>All figures: million GBP per year</b>	<b>Total Admin or Purchasing Cost</b>	<b>Total Import value</b>	<b>Total costs as % of import value</b>
<b>Scenario 2 added purchasing product cost</b>	146.6	6,344.1	2.3%
<b>Scenarios 2.1 and 2.4 admin cost</b>	41.58	6,344.1	0.01%
<b>Scenarios 2.1 and 2.4 one-off set up admin cost</b>	6.67	6,344.1	<0.01%
<b>Scenarios 2.2 and 2.5 admin cost</b>	27.98	6,344.1	<0.01%

<b>Scenarios 2.2 and 2.5 one-off set up admin cost</b>	4.42	6,344.1	<0.01%
<b>Scenarios 2.3 and 2.6 admin cost</b>	13.99	6,344.1	<0.01%
<b>Scenarios 2.3 and 2.6 one-off set up admin cost</b>	2.21	6,344.1	<0.01%

\* UK sourced wood product figures are not shown as there are no additional purchasing costs required. Administration costs are not included as the total is just GBP 17,00 for UK. These figure do not include flooring or board products which would result in a higher total cost.

## Breakdown of impact assessment by wood product sub-sector

### 1. Softwood logs, sawnwood and veneer

Table 2: Annual costs plus set-up costs for softwood logs, sawnwood and veneer

<b>Softwood Logs, Sawnwood and Veneer (Scenario 2)</b>				
		<b>Scenario 2.1 70% due diligence added cost (000 GBP)</b>	<b>Scenario 2.2 80% due diligence added cost (000 GBP)</b>	<b>Scenario 2.3 90% due diligence added cost (000 GBP)</b>
<b>Large companies administration</b>	Annual admin rate (importers)	106	65	33
	Set up cost (importers)	27	17	8
<b>SME administration</b>	Annual admin rate (importers)	360	235	118
	Set up cost (importers)	54	35	18
<b>Additional scenario 2 product cost</b>		10,842	10,842	10,842
<b>GBP</b>	<b>Total additional scenario cost</b>	<b>11,389</b>	<b>11,159</b>	<b>11,019</b>
	<b>Cost per 000 m<sup>3</sup></b>	<b>1</b>	<b>1</b>	<b>1</b>

Total applicable company numbers are: 42 large companies and 172 SMEs. (Applicable companies refer to importing companies, acting as 'first placers' and requiring due diligence). Scenarios 2.1, 2.2 and 2.3 refer to the level of due diligence assumed to be already in place.

## 2 Hardwood logs, sawnwood and veneer

Table 3: Annual costs plus set-up costs for hardwood logs, sawnwood and veneer

Hardwood Logs, Sawnwood and Veneer		Scenario 2.1 70% due diligence added cost (000 GBP)	Scenario 2.2 80% due diligence added cost (000 GBP)	Scenario 2.3 90% due diligence added cost (000 GBP)
Large companies administration	Annual admin rate (importers)	41	25	16
	Set up cost (importers)	10	6	4
SME administration	Annual admin rate (importers)	145	97	48
	Set up cost (importers)	54	15	7
Additional scenario 2 product cost		2,824	2,824	2,824
<b>Total additional scenario cost (GBP)</b>		<b>3,074</b>	<b>2,967</b>	<b>2,899</b>
<b>Cost per 000 m<sup>3</sup></b>		<b>3</b>	<b>3</b>	<b>3</b>
<b>Cost per tonne (other hardwood*)</b>		<b>3</b>	<b>3</b>	<b>3</b>

\*There is a range of products – primarily planed, sanded, finger-jointed sawnwood – where the data is available in tonnes rather than cubic metres. This is included in this additional analysis on the higher due diligence basis due to the product type.

Total applicable company numbers are estimated at: 17 large companies and 70 SMEs.

## 3. Plywood and board products

No additional information

#### 4. BJC products

Table 4.: Annual costs plus set-up costs for builders' joinery and carpentry (BJC) products

<b>Builders' Joinery and Carpentry (BJC)</b>		<b>Scenario 2.4 25% due diligence added cost (000 GBP)</b>	<b>Scenario 2.5 50% due diligence added cost (000 GBP)</b>	<b>Scenario 2.6 75% due diligence added cost (000 GBP)</b>
<b>Large companies administration</b>	Annual admin rate (importers)	56	303	155
	Set up cost (importers)	116	77	39
<b>SME administration</b>	Annual admin rate (importers)	7,782	5,188	2,594
	Set up cost (importers)	1,166	777	389
<b>Additional scenario 1 product cost</b>		15,246	15,246	15,246
	<b>Total additional scenario cost (GBP)</b>	<b>24,365</b>	<b>21,590</b>	<b>18,423</b>
	<b>Cost per tonne (GBP)</b>	<b>0.05</b>	<b>0.04</b>	<b>0.04</b>

Total applicable company numbers are estimated at: 50 large companies and 1500 SMEs. These figures were arrived at by assuming that half of the large companies would require a due diligence process and 30% of the SMEs.

#### 5: Flooring products

No additional analysis.

**6. Wooden furniture**

Table 5 : Annual costs plus set-up costs for wooden furniture

Furniture		Scenario 2.4 25% due diligence added cost (000 GBP)	Scenario 2.5 50% due diligence added cost (000 GBP)	Scenario 2.6 75% due diligence added cost (000 GBP)
<b>Large companies administration</b>	Annual admin rate (importers)	2,250	1,497	744
	Set-up cost (importers)	570	379	189
<b>SME administration</b>	Annual admin rate (importers)	28,056	18,711	9,352
	Set-up cost (importers)	4,202	2,802	1,401
<b>Additional scenario 2 product cost</b>	UK	n/a	0	0
	<b>Total additional scenario cost</b>	137,807	126,120	114,416
	<b>Cost per tonne</b>	<b>0.03</b>	<b>0.03</b>	<b>0.03</b>

Total applicable company numbers are estimated at: 367 large companies and 5,411 SMEs. These figures were arrived at by assuming that considering the 7,000 manufacturing companies separately to the other companies in the supply chain (including the retail sector) due to the larger proportion that is assumed to be importing products directly.

The 75,000 companies that are assumed to operate in the furniture sector do not appear to be based on current figures and this number is widely perceived to be overestimated. Therefore a total figure of 60,000 has been assumed.

It has further been assumed that two thirds of the manufacturing companies dealing in wood components or products. This number is further reduced by one third to account for companies that are neither ‘first placers’ nor importers.

Out of the remaining 60,000 companies in the supply chain ending at retail companies, three quarters are estimated not to deal in wood products with a further two thirds not considered as ‘first placers’ for imported items.

## 7. Other products

Table 6 : Annual costs plus set up costs for 'other' wood products

<b>Fuelwood, charcoal, frames, boxes and barrels</b>				
		<b>Scenario 2.4 25% due diligence added cost (000 GBP)</b>	<b>Scenario 2.5 50% due diligence added cost (000 GBP)</b>	<b>Scenario 2.6 75% due diligence added cost (000 GBP)</b>
<b>Large companies administration</b>	Annual admin rate (importers)	417	278	139
	Set up cost (importers)	106	70	35
<b>SME administration</b>	Annual admin rate (importers)	1,418	948	470
	Set up cost (importers)	212	142	70
<b>Additional scenario 2 product cost</b>		3172	3172	3172
	<b>Total additional scenario cost</b>	<b>5,325</b>	<b>4,610</b>	<b>3,887</b>
	<b>Cost per tonne</b>	<b>0.02</b>	<b>0.02</b>	<b>0.01</b>

Total applicable company numbers are estimated at: 68 large companies and 274 SMEs.

Further market research has revealed that, according to the National Cooperaage Federation, 90% of all the barrels are recycled products and so would not be applicable under the proposed legislation. The replacement 'tops' that are required are manufactured by a small number of UK companies which appear to have a form of due diligence process in place.

Many of the products under this category are liable to be available from furniture or garden centre outlets which are already included in previous categories.

According the Logpile<sup>27</sup> project, there are two industry sectors which are most likely to be affected by the proposed legislation and these include the coal sector including power stations and coal companies selling wood burning products. The last sector includes companies dealing in densified wood products such as pellets.

Information from the Solid Wood Fuel Association revealed that around 300 coal merchants sell wood burning products with the majority importing wood products. A further 30 coal merchants sell wood pellets.

<sup>27</sup> <http://www.nef.org.uk/logpile/>

## 8. Pulp and paper

Table 7 : Annual costs plus set-up costs for pulp and paper products

<b>Pulp and paper</b>		<b>Scenario 2.1 70% due diligence added cost (000 GBP)</b>	<b>Scenario 2.2 80% due diligence added cost (000 GBP)</b>	<b>Scenario 2.3 90% due diligence added cost (000 GBP)</b>
<b>Large companies administration</b>	Annual admin rate (importers)	123	82	41
	Set up cost (importers)	31	21	10
<b>SME administration</b>	Annual admin rate (importers)	830	553	277
	Set up cost (importers)	124	83	41
<b>Additional scenario 2 product cost</b>		18,286	18,286	18,286
	<b>Total additional scenario cost</b>	<b>19,394</b>	<b>19,025</b>	<b>18,655</b>
	<b>Cost per 000 tonne</b>	<b>2</b>	<b>2</b>	<b>2</b>

Total applicable company numbers are estimated at: 50 large companies and 400 SMEs.