

Developing EU measures to
address forest-risk commodities

What can be learned from EU regulation of other sectors?

A Fern discussion paper



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Executive summary

Regulating forest-risk commodities

The EU is one of the largest drivers of tropical deforestation. Consumption of agricultural commodities in particular has given the EU a huge and largely unacknowledged footprint in the rainforests. The EU has recognised that it has to reduce its forest footprint. To do this, the EU must develop measures to address global deforestation by regulating European trade and consumption of forest-risk commodities such as soy, palm oil, beef, leather and cocoa.

The EU has already regulated supply chains in other sectors such as illegal timber, conflict minerals and illegal fishing. This discussion paper looks at what lessons we can learn from the regulation of these supply chains for the development of new EU measures to regulate forest-risk commodities.

Two key issues when regulating

Any forest-risk commodity regulation must take account of two realities. First, the conversion of forest land to large-scale agricultural production is the primary cause of deforestation. Therefore any regulation of forest-risk commodities must deal with this conversion in order to be effective in halting global deforestation. Of particular concern is whether land-use decisions respect the tenure and use rights of indigenous peoples and local communities as well as the environmental and other social impacts of the land conversion.

The second reality is that the global supply chains for the commodities in question are very complex. They entail the amalgamation of materials from multiple sources prior to their incorporation into products retailed in the EU, giving rise to significant traceability challenges. The analysis, findings, and recommendations in this paper focus on how the regulatory frameworks examined might be adapted to respond effectively to these realities.

Illegal fishing

Illegal, unreported and unregulated (IUU) fishing is a major threat to livelihoods, food security, and ocean health globally. In 2008, the EU adopted the EU Regulation to end IUU fishing to shut out illegal catch from the EU market. The Regulation has been in effect since 2010. The regulation includes two demand-side measures: a catch certification scheme which relies explicitly on official documentation from flag states attesting to legality compliance by vessels and an IUU vessel list which bans importation of fishery products from vessels known to engage in IUU fishing. On the supply side, the IUU regulation innovates a 'third-country carding scheme' whereby, if a country fails to implement relevant international agreements, the EU can impose a trade ban on the country's fisheries products. The IUU regulation also imposes penalties on EU nationals who engage in or support IUU fishing anywhere in the world, under any flag.

The IUU regulation's supply-side and demand-side measures warrant close consideration with a view to how they might be adapted to forest-risk commodities. The IUU vessel list is a tool to 'blacklist' imports from suppliers known to be operating illegally. A mechanism for blacklisting the importation of forest-risk commodities from illegally converted plantations or other links in the supply chain that are known to routinely trade in illegally-sourced commodities could be

considered. The IUU regulation's provisions for sanctioning EU nationals who engage in or benefit from IUU fishing could potentially be adapted to cut off financing for the illegal conversion of forest land to large-scale agriculture.

The 'third-country carding scheme' is a mechanism that could be looked at as an option to address the governance and law enforcement issues underlying forest conversion to large-scale agricultural production of forest risk commodities.

Conflict minerals

In certain developing countries the control, extraction, processing and trade of natural resources are financing armed groups who commit serious violations of human rights rather than contribute to human development. In response to global concern, the Organization for Economic Co-operation and Development (OECD) developed the *OECD Due Diligence Guidance for Responsible Supply Chains and Minerals from Conflict-Affected and High-Risk Areas* in May 2011. The OECD guidance clarifies how companies can identify and better manage risks throughout the entire mineral supply chain. It has become the leading industry standard for companies looking to live up to the expectations of customers and of the international community on mineral supply chain transparency and integrity, has been endorsed by 53 countries and forms the basis of laws in other countries including the US and the Great Lakes Region of Africa, as well as guidance developed by the Chinese government for Chinese companies.

The EU is set to adopt a conflict minerals regulation based on the OECD guidelines. In addition to aligning with widely endorsed international norms and standards, the conflict minerals regulation models another important lesson for new EU measures to address forest-risk commodities. The regulation bifurcates supply chains into upstream and downstream operators on either side of key 'choke points' at which supplies from numerous and varied sources are amalgamated. Imposing separate due diligence obligations to upstream and downstream operators helps to overcome the problem of tracing supplies through these choke points.

The new EU conflict minerals regulation also provides for the provision of 'white lists' of responsible supply chain operators to aid operators' due diligence efforts. However, the regulation fails to adequately set out criteria by which whitelisted operators would be selected and monitored.

The new EU conflict minerals regulation would allow existing industry schemes to be recognised as providing compliance with the regulation. When the EU expressly recognises certain schemes as providing compliance with a due diligence regulation, this can, however, undercut the process of continual improvement by allowing an industry-regulated scheme to take the place of a company's individual responsibility to carry out and report on its due diligence. This would create a 'liability loophole' where the failure of an approved certification schemes does not result in liability on the part of the company relying on it, and should be avoided when developing a regulation for forest-risk commodities.

Recommendations

- International law and guidance pertaining to customary tenure and use rights could be referenced as the basis for due diligence obligations imposed on supply chain operators for forest-risk commodities.
- Further work is required to translate the key rights and principles articulated in international laws and guidance documents to frame a due-diligence risk-assessment and risk-mitigation framework. Three of the key principles could be: (1) land use decisions must guarantee the Free, Prior, and Informed Consent (FPIC) of all potentially affected communities through the entire lifecycle of the project; (2) no conversion of contested land; (3) no violation of human rights in the acquisition or management of the land.
- The same measures that would address illegal conversion could also advance the EU Action Plan on Human Rights and Democracy. Objectives 17, 18, and 25 of the Human Rights Action Plan are particularly relevant.
- A due diligence framework for ‘deforestation free’ palm oil, soy, and other forest-risk commodities should be aligned with, and inform, best standards and practices being adopted globally.
- Supply-side measures along the lines of the third-country carding process implemented in the IUU Regulation should be explored and considered as a way to influence governance reforms in producer countries.
- How the existing IUU Regulation’s measures are being implemented on the ground, the challenges encountered, and successes achieved should be examined.
- If measures to address forest-risk commodities include the development of white lists comprised of suppliers deemed ‘responsible’ (or ‘legal’ or ‘sustainable’), listed operators in producer countries should be subject to community monitoring. Inputs from community monitoring efforts should be taken into consideration in determining whether operators should remain whitelisted.
- Regulations should be proposed that would require Member State competent authorities to investigate and prosecute EU nationals or EU-based companies that benefit from illegal land conversion in producer countries by financing or operating surrogate companies in third countries. This regulation could include provisions similar to those in the IUU Regulation.
- Mandatory due diligence obligations should be imposed on both upstream and downstream operators in forest-risk commodity supply chains. For supply chains that typically include key choke points at which supplies from numerous and varied sources are amalgamated in the course of processing and refinement, separate due diligence obligations could apply to upstream and downstream operators, along the lines of the OECD conflict minerals guidelines. This could help to overcome the problem of tracing supplies through the choke points.
- Due diligence should remain the responsibility of economic operators trading in forest-risk commodities. While third-party certification schemes can be a useful tool for due diligence, it is important that certification not be equated with due diligence. In this way, the measures will avoid providing a ‘liability loophole’ and ensure that the due diligence obligations incentivise continual improvement.

Acronyms

3TG	Tungsten, Tantalum, Tin and Gold
CBD	Convention on Biological Diversity
CFP	Common Fisheries Policy
CITES	Convention on International Trade in Endangered Species
ESCR	Economic, Social, and Cultural Rights
EUTR	European Union Timber Regulation
FAO	UN Food and Agriculture Organization
FAR	Fishing Authorization Regulation
FLEGT	Forest Law Enforcement, Governance and Trade
FSC	Forest Stewardship Council
GMOs	Genetically Modified Organism
IUU	Illegal, Unreported and Unregulated
NAPs	National Action Plans
OECD	Organisation for Economic Cooperation and Development
RFMO	Regional Fisheries Management Organization
UNDRIP	United Nations Declaration of the Rights of Indigenous Peoples
UNFCCC	United Nations Framework Convention on Climate Change
UNGPs	UN Guiding Principles on Business and Human Rights
VGGT	Voluntary Guidelines on the Governance of Tenure
VPA	Voluntary Partnership Agreement

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Introduction

The EU must develop measures to address global deforestation by regulating European trade and consumption of forest-risk commodities such as soy, palm oil, beef, leather and cocoa. This paper examines trends in the regulation of consumer products driven by sustainability concerns. It highlights measures adopted (or being developed) by the EU to regulate trade in timber, fish and minerals. These new regulatory frameworks may offer valuable lessons for the development of new EU measures to regulate forest-risk commodities.

This analysis is based on desk research and was developed with two important realities about forest-risk commodities in mind. The first reality is that the conversion of forest land to large-scale agricultural production is the primary cause of deforestation. Therefore any regulation of forest-risk commodities must relate to this conversion in order to be effective in halting global deforestation. Of particular concern is whether land-use decisions respect the tenure rights of indigenous peoples and local communities as well as the environmental and other social impacts of the land conversion. The second reality is that the global supply chains for these commodities are very complex. They entail the amalgamation of materials from multiple sources prior to their incorporation into products retailed in the EU, giving rise to significant traceability challenges. The analysis, findings, and recommendations in this paper focus on how the regulatory frameworks examined might be adapted to respond effectively to these realities.

Following a survey of existing EU regulatory frameworks, including those governing the illicit arms trade, and trade in seal products, GMOs, textiles, illegal wildlife, biofuels and biomass, this paper focuses on those deemed most relevant and transferable in light of these realities: the frameworks governing trade in timber, fishery products, and conflict minerals. Accordingly, only these frameworks are discussed in detail in this paper. It is assumed that those interested in the development of EU measures to tackle global deforestation through the regulation of forest-risk commodities will already be familiar with the existing EU framework regulating trade in illegal timber, and therefore this framework is not described at length here. However, comparative references to FLEGT VPA processes, FLEGT licensing systems and the EU Timber Regulation are made throughout the paper.

Section 1 provides an introduction to supply- and demand-side approaches to regulating commodities for sustainability purposes. It explains why due diligence frameworks are generally preferable to policies seeking to certify products (or supplies) as ‘legal’ or ‘sustainable’. **Section 2** explores the EU’s regulatory framework for illegal, unreported and unregulated (IUU) fishery products. **Section 3** looks at the regulatory framework for conflict minerals recently agreed by EU lawmakers. **Sections 2 and 3** each conclude with an analysis of how the framework could be adapted to forest-risk commodities. **Section 4** provides a summary analysis of the lessons that Fern and its allies can apply to the development and advocacy of ambitious, appropriate, and feasible EU measures to address deforestation. Finally, **section 5** recommends next steps to deepen our understanding of the frameworks from which this paper draws key lessons, not only to better understand their design, but also the on-the-ground political battles waged to adopt them, the implementation challenges encountered, and successes achieved.

1 Supply-side and demand-side measures

Measures to regulate consumer products for sustainability purposes can take the form of supply-side measures or demand-side measures.

1.1 Supply-side measures

Supply-side measures aim to foster better governance of natural resources in producer countries by building the country's governance capacity and performance. Environmental advocates generally agree that improved governance is required to ensure a meaningful and broad shift towards more sustainable management of natural resources, and therefore improved governance should be an ultimate aim of any measure to regulate commodities for sustainability purposes. Examples of supply-side measures include the 'third-country carding system' component of the IUU fishing regulation as well as FLEGT VPA processes to improve forest governance in the context of timber-trade agreements between the EU and timber-producing countries. In the case of forest-risk commodities, supply-side measures should foster governance improvements aimed at ensuring that land-use decisions respect the tenure and use rights of indigenous peoples and local communities. This is important not only to respect human rights, but also because it has been demonstrated that strengthened tenure rights contribute to more sustainable resource management.¹

1.2 Demand-side measures

Demand-side measures influence the sustainable management of natural resources more indirectly by requiring those who trade commodities to evaluate their supply chains in line with specified standards or principles and to only trade products that comply. Demand-side measures can provide an important incentive for producer countries to improve their governance of the sector, because compliance with a consumer country's demand-side measure is required to ensure access for the producer country's products into the consumer country's market.

Existing demand-side measures generally fall into one of two categories. The first are measures that rely on official documentation from the producer country government as conclusive evidence of the product's compliance with the principles set out. Examples include CITES, the IUU Regulation's fish certification scheme, the EU seal products regime, and the EU FLEGT Regulation. Under these schemes, unless the producing country government's documentation attesting to compliance is found to be fraudulent, it will be accepted by EU officials as proof of compliance. The second category comprises mandatory due diligence schemes, in which EU operators trading the commodity are required to assess the risk that the traded products fail to comply with the principles specified in the regulation. Examples include the EU Timber Regulation and some components of the proposed conflict minerals regulation. Some EU measures are essentially a hybrid, as exemplified by the pending conflict minerals regulation, which requires due diligence on the part of importers of certain minerals and ores, but also provides for industry schemes to be formally recognised by the EU as providing compliance with the regulation.

¹ See sources cited in notes 21 and 22, below.

2 Fish

Illegal, unreported and unregulated (IUU) fishing is a major threat to livelihoods, food security, and ocean health globally. Between 11 and 26 million tonnes of fish are caught illegally per annum. It is estimated that this amounts to between 13 and 31 per cent of reported fisheries production and results in an estimated economic loss from IUU Fishing of \$10 to \$23.5 billion USD per year.² IUU fishing is one of the main impediments to achieving legal and sustainable fisheries at a time of mounting threats to marine biodiversity and food security.

Fisheries in the territorial waters of EU Member States are regulated by the EU Common Fisheries Policy (CFP). Vessels carrying the flags of EU Member States are regulated by the EU Fishing Authorization Regulation (FAR). Many of the fishery products consumed in the EU come from sources not directly regulated by the EU, however. The EU is the world's largest importer of fishery products, importing many high-value products via trading partners around the world, and thus is a valuable destination for IUU operators. In 2008, the EU adopted the EU Regulation to end illegal, unreported and unregulated (IUU) fishing³ to shut out illegal catch from the EU market. The regulation has been in effect since 2010.

2.1 The IUU Regulation

The IUU Regulation has four components:

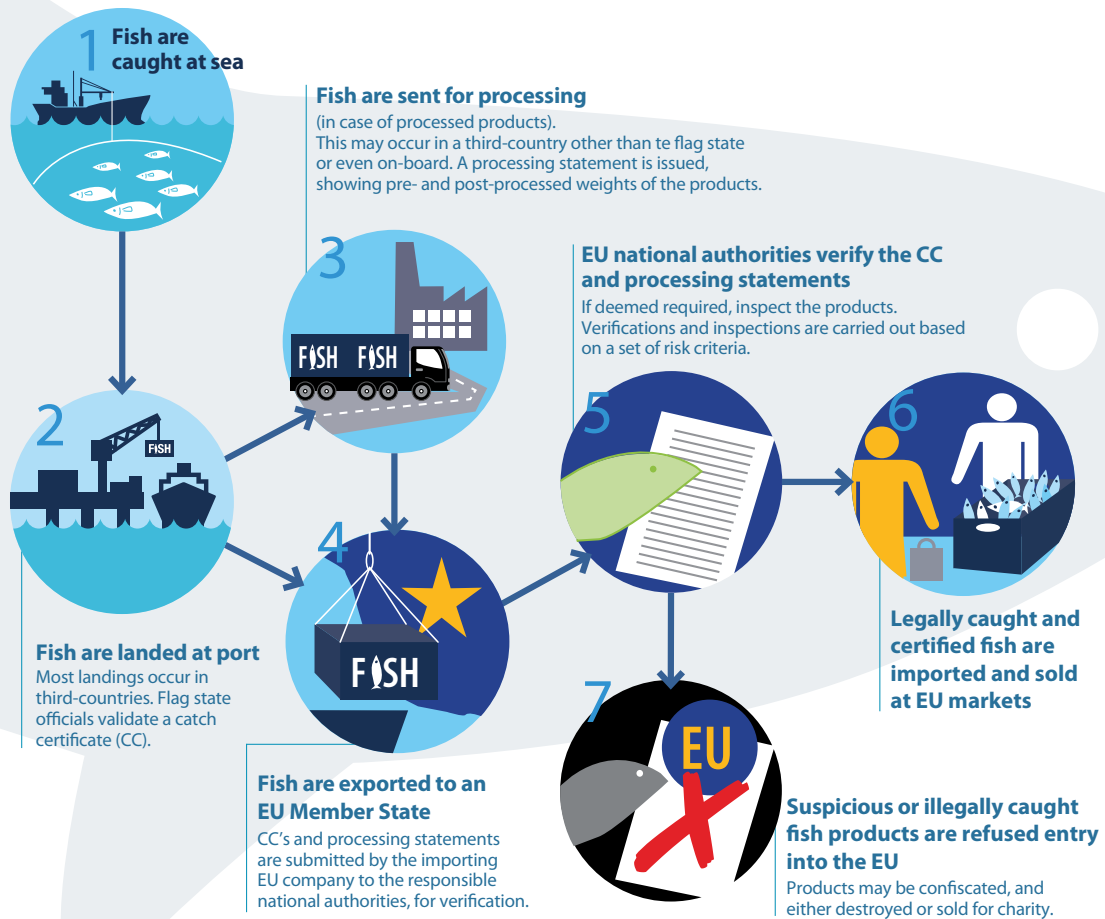
1. **Catch certification scheme:** Only marine fishery products validated as legal by the competent flag state⁴ can be imported to or exported from the EU.
2. **Third-country carding system:** The Regulation enables the EU to enter into dialogue with non-EU countries that are not combatting IUU fishing effectively. If third countries fail to put in place required reforms in a timely manner, then sanctions – including trade bans on the country's fisheries products – can be imposed.
3. **Penalties for EU nationals:** EU nationals who engage in or support IUU fishing anywhere in the world, under any flag, face substantial penalties proportionate to the economic value of their catch. These sanctions deprive them of any profit, thereby undermining the economic driver of their illegal actions.
4. **IUU vessel list:** The regular publication of an IUU vessel list based on lists of IUU vessels identified by Regional Fisheries Management Organisations (RFMOs) as vessels engaged in IUU fishing. Listed vessels are barred from landing at the ports of EU Member States except in emergency.

2 Agnew D.J., et al., *Estimating the Worldwide Extent of Illegal Fishing*, PLoS ONE 4(2): e4570. doi: 10.1371/journal.pone.0004570 (2009).

3 Council Regulation (EC) No. 1005/2008: <http://eur.lex.europa.eu/legal-content/EN/TXT/?qid=1408984470270&uri=CELEX:02008R1005-20110309/>.

4 The flag state is the state in which the vessel is registered.

Figure 1: IUU Regulation's Catch Certification Scheme



Reproduced from The EU IUU Regulation: Building on success, EU progress in the global fight against illegal fishing (Environmental Justice Foundation, Oceana, Pew Charitable Trusts, and WWF, February 2016).

2.1.1 Catch certification scheme

The IUU Regulation requires flag states to certify the origin and legality of the fish by means of a catch certificate. The Regulation applies to all landings and transshipments of EU and third-country fishing vessels in EU ports, and all trade of marine fishery products (excluding aquaculture products) to and from the EU, thereby facilitating the traceability of all marine fishery products traded from and into the EU. Where fish are processed and potentially mixed with fishery products from other sources, a processing statement is issued, showing pre- and post-processing weights of the products. **Figure 1** illustrates the steps to be taken under the IUU Regulation by flag states and EU Member States into which fishery products are imported.

For the purposes of the IUU Regulation, legality is understood as compliance with all the flag state's own conservation and management rules and also with internationally agreed rules applicable to the fishery concerned. As a preliminary step, countries must notify the European Commission that they have the necessary legal instruments, the dedicated procedures, and the appropriate administrative structures in place for the certification of catches by vessels flying their flag. To date, 90 countries have done so.

Some of the largest importing EU Member States receive between 40,000 and 60,000 catch certificates per year (between 110 and 165 per day).⁵ Many of these are paper-based, or scanned copies of paper certificates. Reliance on a paper-based system poses the risk that some of the certificates presented will be fraudulent. Therefore competent authorities in the Member States must have a system for checking that catch certificates provided by vessels in their ports really were issued by the flag state. Of course it is not possible for Member State competent authorities to individually verify the information on every certificate. So a risk-based approach to the verification of catch certificates is applied to ensure that rigorous and stringent verifications are focused on those imports that are most at risk of being a product of IUU fishing activities. Risk factors include species of high commercial value, or consignments originating from vessels, regions, or companies with known IUU fishing histories.

Of course, catch certificates issued by a flag state will only be credible if the flag state has a robust system for monitoring and verifying legal fishing as well as sufficiently deterrent sanctions for those acting illegally. These considerations are taken up through the third-country carding system.

2.1.2 Third-country carding system

The IUU Regulation requires that countries which export fish to the EU, or which lend their flags to vessels that are involved in the EU supply chain, must cooperate in the fight against IUU fishing. Under the Regulation, the European Commission conducts fact-finding missions to evaluate the compliance of third countries with their duties as flag, coastal, port, or market states under international law.⁶ Notably, the international laws governing marine fisheries are fairly well developed and include the United Nations Convention on the Law of the Sea, the FAO International Plan of Action to Prevent, Deter and Eliminate IUU fishing, and the United Nations Fish Stocks Agreement. A UN Port State Measures Agreement, the world's first ever binding international accord specifically targeting IUU fishing, was recently ratified by 25 countries and came into force on 5 June 2016.⁷ In addition, several RFMOs have been agreed to jointly manage fisheries in marine regions which do not fall within any country's territorial waters. These international and regional agreements are further supplemented by the FAO Voluntary Guidelines for Flag State Performance.

Where a country's governance capacities and performance are deemed insufficient, the EU will attempt to engage with the country to help foster improvements, including through the provision of capacity building resources. Where the country is found to be non-cooperative or otherwise fails to make sufficient improvements, the EU will first issue a warning (yellow card) formally setting out the improvements needed in order to maintain access to the EU market for the flag state's vessels. In the most severe cases of non-performance, the EU will issue a red card, banning the import of fishery products from any of the flag state's vessels. Granting a red card consists of two steps. First, the Commission proposes the red card, setting out the evidence on which its recommendation is based. Second, the Council of the EU adopts the decision to issue a red card and apply sanctions to the third country. On making required improvements, a country can be delisted (green card).

5 *The EU IUU Regulation: Building on success, EU Progress in the global fight against illegal fishing* (Environmental Justice Foundation, Oceana, Pew Charitable Trusts, WWF, February 2016) at 7, available at [http://ejfoundation.org/report/EU-IUU-Regulation-Coalition \(Building on Success\)](http://ejfoundation.org/report/EU-IUU-Regulation-Coalition%20Building%20on%20Success).

6 Article 3 of the IUU Regulation.

7 *International Law Tightens Grip on Illegal Fishing* (Huffington Post, 23 May 2016), available at <http://www.iuuwatch.eu/2016/05/international-law-tightens-grip-on-illegal-fishing/#more-1373> and *Ground Breaking IUU Accord Soon to Enter Force* (FAO, 16 May 2016), available at <http://www.iuuwatch.eu/2016/05/ground-breaking-illegal-fishing-accord-soon-to-enter-into-force/#more-1349>

The first step is for the Commission and third-country authorities to enter into a dialogue, which can last for months or even years, to assess the systems in place to prevent IUU fishing and their compliance with international rules according to the following criteria:

- Ratification of international instruments and participation in regional and multilateral cooperation, including membership of RFMOs and compliance with RFMO conservation and management measures (e.g. with regard to reporting, observers, and lists of authorised vessels).
- Compliance of a third country's legal framework with international and regional fisheries management and conservation requirements (e.g. the registration of vessels, systems for monitoring, inspection and enforcement, and effective sanctions).
- Implementation of appropriate fisheries and conservation measures, allocation of adequate resources, and establishment of systems necessary to ensure control, inspection and enforcement of fishing activities both within and beyond sovereign waters (e.g. an accurate licensing system and updated list of authorised vessels).

In considering these issues, the Commission takes into account the constraints of developing countries and the existing capacity of their competent authorities, particularly in relation to the monitoring, control and surveillance of fishing activities.⁸ The dialogue provides a framework for the EU to provide capacity-building and technical assistance to strengthen fisheries' management and control in third countries.

A decision to issue a red or yellow card is based on a body of evidence developed by the European Commission citing specific violations of relevant international and regional agreements, and recommending the steps that carded countries must take to remedy them. Carded countries must demonstrate clear indications of genuine political will to address illegalities, adopt appropriate regulatory frameworks and, most importantly, design and adopt systems to implement and monitor the necessary law and governance reforms. In addressing cited violations, each carded country must account for its specific characteristics – for example, the size and scope of its fishing industry, exclusive economic zone, and processing sector. The commission has cited the following areas of concern repeatedly in its carding decisions:⁹

- **Legal gaps:** Some countries fail to ensure that their fisheries laws are consistent and fully implemented.
- **Lack of control over vessels:** Countries are accountable for the actions of boats fishing under their flags. Some nations do not maintain up-to-date ship registers or ensure sufficient monitoring, control and surveillance of their fleets.
- **Poor conservation measures and/or fisheries management structures:** These must be clear, transparent, based on current science, and consistent with international obligations.
- **Failure to cooperate with regional and multilateral bodies:** The EU wants importing states to work with RFMOs on fishing and stock management; some neglect to do so.
- **Traceability and fish processing:** Flag states and the countries that process fish should

⁸ Article 31(5)(d) and 31 (7) of the IUU Regulation.

⁹ *New Analysis Highlights Common Failures in Managing Illegal Fishing* (Pew Charitable Trusts, June 2016) and reports cited therein, available at <http://www.iuuwatch.eu/2016/06/new-analysis-highlights-common-failures-in-managing-illegal-fishing/#more-1389>

Figure 2: IUU Regulation Third-Country Carding Process

How does the carding process work?



Reproduced from *The EU IUU Regulation: Building on success, EU progress in the global fight against illegal fishing* (Environmental Justice Foundation, Oceana, Pew Charitable Trusts, and WWF, February 2016).

cooperate to document the origin and supply chain journey of catch and ensure the legality of processed products. Some parties have failed to achieve this.

To date, the EU has engaged with almost 50 countries seeking improvements in measures to combat IUU fishing. The majority have undertaken key reforms recommended by the EU with no need for warnings. Twenty countries have received yellow cards to improve their fisheries management, of which nine have undertaken robust reforms and been delisted. Four countries have been issued with a red card, which means a ban on their fish products entering the EU. Two of these countries – Cambodia and Guinea – remain red-carded as of July 2016, while Belize was delisted in December 2014 and Sri Lanka in June 2016.¹⁰

¹⁰ Commission Implementing Decision as of 26 November 2013 identifying the third countries that the Commission considers as non-cooperating third countries pursuant to Council Regulation (EC) No 1005/2008 establishing a Community system to prevent, deter and eliminate illegal unreported, and unregulated fishing, C346/2 Official Journal of the European Union, 27 November 2013; Council Implementing Decision of 24 March 2014 establishing a list of non-cooperating third countries in fighting IUU fishing pursuant to Council Regulation (EC) No 1005/2008 establishing a Community system to prevent, deter and eliminate illegal unreported, and unregulated fishing, Official Journal of the European Union, 27 March 2014; Council Implementing Decision of 15 December 2014 amending Implementing Decision 2014/170/EU establishing a list of non-cooperating third countries in fighting IUU fishing pursuant to Council Regulation (EC) No 1005/2008 establishing a Community system to prevent, deter and eliminate illegal unreported, and unregulated fishing as regards Belize, Official Journal of the European Union, 17 December 2014; Council Implementing Decision of 16 June 2016 amending non-cooperating third countries in fighting IUU fishing pursuant to Council Regulation (EC) No 1005/2008 establishing a Community system to prevent, deter and eliminate illegal unreported, and unregulated fishing, Official Journal of the European Union, 21 June 2016.

2.1.3. Penalties for EU nationals and operators

The IUU Regulation requires Member States to penalise any EU individual or EU-based entity proven to have been involved in IUU fishing and related trade with effective, proportionate and dissuasive sanctions. This relates to cases where EU-flagged vessels have been found responsible for IUU fishing, where non-EU flagged vessels have been traced back to EU ownership; and where EU nationals benefit financially from IUU profits. In other words, the IUU Regulation prohibits all EU nationals from engaging in or supporting IUU fishing activities under any flag, whether directly or indirectly, and provides for sanctions in case of violation of these provisions. In the event of serious infringements, EU Member States must impose a sanction of at least five times the value of the fishery products obtained through committing the offence, and eight times the value of the fishery products in case of a repeated infringement within a five-year period.

2.1.4. IUU vessel list

The IUU Regulation requires the European Commission to publish and update a list of vessels identified by RFMOs as engaging in IUU fishing. Listed vessels are barred from landing at the ports of EU Member States. If a flag state tends to have a lot of vessels on the IUU vessel list, then other vessels from that flag state will be more likely to be checked under Member States' risk-based assessment to prioritise their checks on catch certificates. The IUU vessel list is also an important indicator for the third-country carding system, particularly where the flag state fails to sanction listed vessels.

2.2 Effectiveness of the IUU Regulation

The IUU Regulation was adopted by the EU in 2008 and has been in effect since 2010. Every two years, Member States are required to transmit a report to the Commission on the application of the IUU Regulation and, on the basis of these reports, the Commission draws up a report every three years to be submitted to the European Parliament and the Council. Moreover, the regulation specifies that the Commission shall undertake an evaluation of the impact of the regulation by 29 October 2013. The Directorate-General for Maritime Affairs and Fisheries (known in short as DG MARE) published a report fulfilling this requirement in April 2014.¹¹

The implementation of the Regulation has been closely monitored by NGOs including the Environmental Justice Foundation, Oceana, the Pew Charitable Trust, and WWF. In addition to working with NGO partners around the globe to investigate IUU fishing activities and to monitor the Regulation's implementation and enforcement by Member States and the European Commission, these NGOs jointly maintain a website providing information about the IUU regulation, its implementation, and related issues at www.IUUwatch.eu. The NGO coalition published a comprehensive assessment of the IUU regulation in February 2016: *The EU IUU Regulation: Building on success, EU progress in the global fight against illegal fishing*.¹²

The Commission report provides useful statistics on the implementation of the Regulation by Member States with regard to resources allocated, certificates checked, etc. It notes that, because the Regulation had only been in place for a few years prior to the report, its implementation was still a work in progress. The NGO report examines the first five years of the Regulation's

¹¹ DG MARE, *Study on the state of play regarding application and implementation of Council Regulation (EC) No 1005/2008 of 29 September 2008, establishing a community system to prevent, deter, and eliminate illegal, unreported and unregulated fishing (IUU Regulation)* (Final Report, April 2014), available at http://ec.europa.eu/fisheries/documentation/studies/iuu-regulation-application/doc/final-report_en.pdf

¹² *The EU IUU Regulation: Building on success, EU progress in the global fight against illegal fishing ('Building on Success report')* (Environmental Justice Foundation, Oceana, Pew Charitable Trusts, and WWF, February 2016), available at http://www.iuuwatch.eu/wp-content/uploads/2016/02/IUU_report_090216_web.singles.pdf

implementation and takes a more critical perspective. It draws from the data reported by the Commission in 2014 as well as more recent Member State reports, its own investigations, and other stakeholders' concerns. The following analysis draws primarily from the 2016 NGO report.

The NGO report found that 'since its introduction, the regulation has proven a powerful tool to combat IUU fishing' and that it had prevented illegally caught fish entering the EU market and driven positive change in fisheries standards and procedures in countries around the world.¹³ In particular, the report lauds the impact that the third-country carding system has had on encouraging substantial on-the-ground improvements in fishery management standards in third countries. The report noted that producer countries have described the carding system as a strong incentive to align their national policies and legislation with international law and to strengthen their implementation and enforcement of these laws.¹⁴

The Building on Success report also emphasised that the full promise and potential of the IUU Regulation has been compromised by a lack of robust and harmonised implementation of the catch certificate scheme across Member States, leaving scope for abuse.¹⁵ Principal recommendations of the report are for more resources for Member State enforcement of the IUU Regulation, and for more harmonised enforcement across the EU. The report also raises concerns about leakage, and recommends that, to ensure that the IUU Regulation does not simply displace IUU catch to markets with weaker or non-existent regulatory controls, the EU should strengthen its efforts towards multilateral action to address IUU fishing.

The Building on Success report strongly recommended the modernisation of the catch certification scheme through the introduction of an electronic database, incorporating a robust risk assessment tool to standardise the procedure across Member States. It notes that the Commission has committed to delivering such an IT system in 2016.¹⁶ This would improve transparency of fishery supply chains as well as harmonise the implementation of the IUU Regulation across Member States. In addition, an electronic traceability system could help address problems where a certified catchment is split in the course of processing, but then each portion topped up with products from another source (potentially illegal) to equal the amount initially certified.¹⁷

In general, however, the report notes that increased demand for greater traceability of fish catches has been driven by the IUU Regulation and its fostering of compliance with international agreements such as the Port State Measures Agreement and the Voluntary Guidelines for Flag State Performance. Although gaps in traceability systems remain, the IUU Regulation is encouraging the development and adoption of solutions for improved traceability.¹⁸

At the same time, the Building on Success report criticises the lack of action by some Member States to implement the IUU Regulation's provisions to impose sanctions on EU nationals who benefit from IUU fishing, noting that there was little evidence that Member States were actively identifying and prosecuting serious infringements by EU nationals, and several Member States had not even transposed the requirements into national law.¹⁹ However, the report also highlights 'Operation Sparrow', an enforcement action undertaken by Spain, to demonstrate the

¹³ *Ibid.* at 17.

¹⁴ *Ibid.* at 17.

¹⁵ *Ibid.* at 12-15, 17.

¹⁶ *Building on Success* at 16-17. See also *Ensuring legal EU seafood imports: the digital revolution must happen this year* (WWF, 27 April 2016), available at <http://www.iuuwatch.eu/2016/04/ensuring-legal-eu-seafood-imports-the-digital-revolution-must-happen-this-year/#more-1307>

¹⁷ *Ibid.* at 16.

¹⁸ *Lack of Transparency: The Achilles Heel in IUU Fishing Control* (House of Ocean, June 18, 2016), available at <http://www.iuuwatch.eu/2016/06/lack-of-transparency-the-achilles-heel-in-iuu-fishing-control/>

¹⁹ *Ensuring legal EU seafood imports*, *supra* note 18, at 17.

impact the regulation can have on EU nationals complicit in IUU fishing. Operation Sparrow is an ongoing investigation of four vessels suspected of illegally fishing Patagonian toothfish in Antarctic waters. Phase one, which involved raids on company offices and analysis of over 3000 documents, found clear evidence that the companies are connected to the vessels, with multiple very serious infringements of laws. Spanish authorities have so far announced fines against the Spanish operators totaling almost €18 million, more than has ever been imposed by an EU government for IUU fishing.²⁰

2.3 How components of the IUU Regulation might translate to forest-risk commodities

This section compares components of the IUU Regulation to FLEGT VPAs and the EUTR.

2.3.1 Supply-side measures to improve governance: Carding system compared to VPAs

Illegal conversion of forests to large-scale agriculture is the major driver of global deforestation. Widespread illegalities – including violations of community tenure rights – are associated with forest conversion in most of the major source countries for forest-risk commodities.²¹ A general lack of transparency and other features of good governance make it hard to monitor forest conversion and whether these land-use decisions are consistent with all relevant laws. Studies have shown that improving forest and land governance and, in particular, recognising and protecting the rights of local people(s) over forest lands, are two of the most important things that can be done to reduce deforestation.²² Therefore EU measures to reduce deforestation should aim to improve forest governance and recognise and protect the rights of local people over forest lands.

FLEGT VPA processes aim to do this in relation to illegal logging. VPA processes have been criticised for being too time and resource-intensive, however. This section explores whether something along the lines of the IUU Regulation's third-country carding system could provide a less resource-intensive approach that might address the governance and law-enforcement issues underlying forest conversion to large-scale agriculture. Like VPAs, the IUU Regulation's carding scheme aims to encourage EU trading partners to adopt and implement governance reforms aligned with the EU's legality and sustainability concerns. However, the two models differ in some significant ways.

Reliance on existing international laws and norms rather than bilateral trade agreements

FLEGT VPAs are bilateral trade agreements between the EU and timber-producing countries. The definition of 'illegal timber' is clarified within each VPA with reference to the partner country's national laws. Little reference is made to relevant international laws, even where national laws

20 *Building on Success*, supra note 14, at 10. See also *Operation Sparrow brings an important message to the fight against IUU fishing* (House of Ocean, 21 March 2016), available at <http://www.iuuwatch.eu/2016/03/operation-sparrow-brings-an-important-message-to-the-fight-against-iuu-fishing/#more-1262> and *Spanish operation nets suspects behind illegal fishing* (INTERPOL, 18 March 2016), available at <http://www.iuuwatch.eu/2016/03/spanish-operation-nets-suspects-behind-illegal-fishing/>.

21 Sam Lawson, *Consumer Goods and Deforestation: An Analysis of the Extent and Nature of Illegality in Forest Conversion for Agriculture and Timber Plantations* (Forest Trends, September 2014).

22 Britaldo Soares-Filho, et al., *Role of Brazilian Amazon Protected Areas in Climate Change Mitigation*, PNAS 107(24): 10821-10826 (2010). doi:10.1-73/pnas.0913048107 (attributing most of the 70% decline in tropical deforestation in the Brazilian Amazon over the early part of 2004-2012 to the issuance of rights over large tracts of forests to indigenous groups); Eugenio Y. Arima, et al., 'Public Policies Can Reduce Tropical Deforestation: Lessons and Challenges from Brazil' in *Land Use Policy* 41:465-473 (2014). doi:10.16/j.landusepol.2014.06.026 (noting that, from 2008 onwards, actions by government to tackle climate illegal deforestation were the most important factor contributing to the 70% decline in tropical deforestation in Brazil over the period 2004-2012). See also *Consumer Goods and Deforestation*, note 23.

either incorporate or are subordinate to international law. In contrast, the IUU Regulation relies not only on compliance with relevant national laws; it also relies directly on international laws and other international and regional agreements pertaining to illegal fishing. These international and regional agreements are important reference points for the EU's dialogue with third countries about IUU fishing – and potential yellow and red cards. Notably, they include not only international treaties and RFMOs, but also action plans such as the FAO International Plan of Action to Prevent, Deter and Eliminate IUU fishing (which provided the template for the recently adopted UN Port State Measures Agreement) and guidelines such as the FAO Voluntary Guidelines for Flag State Performance.

Many countries will have already signed up to relevant international agreements. If not, then asking countries to ratify these international agreements becomes one of the first steps towards fulfilling the IUU Regulation's conditions for third countries. Where both the EU and another state are both parties to relevant international and regional agreements, this provides a shared set of principles, norms and rules for working together to eliminate IUU fishing. In some cases, the flag state may be a signatory to an international commitment, but has not yet adopted a national legal framework to implement its requirements. But even where a country's laws are compliant 'on paper', this will not be sufficient if the necessary resources and political will needed for their full implementation and enforcement are not forthcoming.

The FLEGT approach of pursuing bilateral agreements to define legal logging in reference to the producer country's national legal framework was largely motivated by concerns about national sovereignty. However, where a producer country has committed to implementing international human rights in line with international law and agreements to which they are a party, such agreements are sovereign decisions which deserve to be fully respected by the signatory country's trading partners. This principle also extends to the EU – that is, adopting EU regulations that require EU trading practices to be aligned with international standards and agreements addressing human rights, sustainable resource management, and climate change mitigation is one way for the EU to fulfill its own commitments under international agreements, and should be respected by the EU's trading partners. This includes defining what the EU will allow to be imported into its market. Insisting on a satisfactory level of compliance by flag states with both the spirit and the letter of these agreements as a basis for accepting imports from the flag state is a logical next step.

Defining international laws relevant to addressing illegal forest conversion

Prior to the adoption of the IUU Regulation, there already was a body of international law concerned with the sustainable management of marine fisheries.^{23,24} This body of international law is further supported by RFMOs which provide more specific rules for and monitoring of fisheries in specific marine areas not regulated as any country's territorial waters. That this area of international law should be relatively well-developed is not surprising, in the light of the unique nature of marine resources as a shared global commons. Not only is much of the ocean outside any single country's territorial reach: even the resources within territorial waters – particularly fish – are intermixed with and influenced by the environmental health and sustainable management of oceans as a whole. Notwithstanding efforts to develop international agreements on the sustainable management of forests, there is no similar body of international law for forest management.

²³ See, for example, the international agreements and RFMOs cited in section 1.1.2, above.

²⁴ Most recently, in June 2016, a UN agreement focusing on IUU fishing – the UN Port State Measures Agreement – was adopted. Although this was after the IUU Regulation, it will automatically be incorporated into the implementation of the IUU Regulation.

As noted above, however, the key issue underlying global deforestation is the conversion of forest land to large-scale agriculture. Such conversion is often illegal because it takes place in violation of the tenure rights of indigenous peoples and local communities or other relevant laws.²⁵ Unlike for forest management or sustainable land use generally, land and resource tenure rights for forest communities are recognised within existing international frameworks.

There is also a growing body of evidence that securing community tenure rights leads to reduced deforestation and more sustainable forest management.²⁶ Accordingly Fern has called for EU measures to address global deforestation that would motivate compliance with human rights laws and other international agreements and guidelines relevant to securing community forest tenure and use rights.²⁷ Relevant treaties may differ depending on the country involved, but could include the International Covenant on Civil and Political Rights; the International Covenant on Economic, Social and Cultural Rights; the International Convention on the Elimination of All Forms of Discrimination against Women; ILO Convention No. 169 on Indigenous and Tribal Peoples; the African Charter on Human and Peoples' Rights; and the American Convention on Human Rights.

Notably, international agreements deemed relevant under the IUU Regulation are not limited to formal, binding international treaties. Voluntary guidelines such as the FAO Voluntary Guidelines for Flag State Performance are also relevant. In the case of forests and customary tenure rights, international standards such as the United Nations Declaration of the Rights of Indigenous Peoples (UNDRIP) and the FAO's Voluntary Guidelines on the Governance of Tenure (VGGT) could provide important measures of compliance with customary tenure and use rights.²⁸

Other international agreements relevant to sustainable forest management and forest governance and related tenure rights include the New York Declaration on Forests and the CBD Action Plan on Customary Sustainable Use, among others. Other important international frameworks and agreements that are not specific to human rights or tenure rights, or forests but which have significant implications for forest governance and management include the UN Framework Convention on Climate Change, including the Paris Agreement and related national commitments, and the UN Sustainable Development Goals. Further work is needed to specify how the provisions in these agreements can be articulated as standards and criteria for EU measures to prevent the conversion of forest land to large-scale agriculture.

The mechanics of the third-party carding system compared to FLEGT VPAs: Banning imports from non-cooperative countries, rather than fostering a 'green lane' for cooperative countries

The mechanics of the IUU Regulation's carding system differ from FLEGT VPAs. The IUU Regulation authorises the European Council, upon recommendation of the Commission, to ban the import of fishery products from non-cooperating countries by issuing a red card. This means that all catches from vessels operating under the flag of a red-carded country are banned. This creates a strong incentive for the flag state to comply with the EU's conditions in order to reopen trade in fishery products with the EU, the largest import market for fishery products in the world.

²⁵ *Consumer Goods and Deforestation*, note 23 above. See also *FPP comments and inputs to EU FLEGT Action Plan evaluation (2003-2014)* (Forest Peoples Programme, August 2015).

²⁶ See *Human Rights and Timber Supply Chains*, note 25 at FN 20, and sources cited therein. See also sources cited in note 24.

²⁷ *Briefing Note: Tackling illegal logging, deforestation and forest degradation: an agenda for EU action* (Greenpeace, Conservation International (Europe), WWF, ClientEarth, Fern, EIA, Forest Peoples Programme, Transparency International (EU Office), Global Witness, March 2016).

²⁸ For a further discussion of international agreements relevant to the illegal conversion of forest land, see *Human Rights and Timber Supply Chains*, note 25, and sources cited therein.

VPA processes are geared towards the development of a timber legality assurance system robust enough to ensure the credible licensing of legal timber. The EUTR prohibits the trading of illegal timber and requires operators placing timber on the EU market to exercise due diligence to reduce the risk of placing illegal timber. The EUTR specifies an exception for FLEGT-licensed timber, providing a 'green lane' for FLEGT-licensed timber into the EU. In this way the EUTR complements, reinforces and motivates VPAs and the strengthened forest governance which is the broader aim of VPA processes. By providing a green lane for FLEGT-licensed timber, the EU rewards governance improvements achieved through VPA processes. But there is nothing in either the FLEGT Regulation or the EUTR that authorises the EU to ban imports from countries deemed high risk for illegal timber, or otherwise lacking in systems and governance to address illegal logging.

Thus, a key difference in the mechanics of the two approaches is the use of carrots vs sticks (incentives and penalties) to encourage desired governance reforms. The IUU Regulation uses red cards as a stick to penalise countries that have poor governance regimes undercutting the goals of the IUU Regulation. In contrast, FLEGT VPAs offer a carrot to countries identified as high risk for trading illegal timber. The FLEGT licensing systems and related law and governance reforms implemented through VPA processes reduce this risk and result in better access for the country's timber exports to the EU market. In both cases, complementary demand-side measures, as well as dialogue and capacity building, are also at work to influence producer countries at various levels of performance along the good governance spectrum.

Under a VPA/EUTR kind of regime, VPA countries are pursuing market-wide governance reforms. But a common avenue for legal actors within non-VPA countries (and in VPA countries until VPA licensing is fully in place) is to pursue a voluntary certification standard such as FSC in order to secure access to the EU market. This allows distinctions to be drawn between the relatively good and bad actors within a national governance framework, which may be very weak. Having secured market access through certification, the motivation of 'good' producers to push from within for stronger governance may not be as great. In contrast, because a red-card ban issued under the IUU Regulation applies to all vessels from the flag state – including those that are not engaged in illegal fishing – the carding system should provide a strong motivation for companies and communities engaged in legal fishing endeavors to pressure their country to adopt nation-wide reforms to come into compliance to remove red and yellow cards.

The investigations and dialogues that precede the imposition of red (and yellow) cards examine similar issues to those at the center of VPA processes. But the unilateral issuance of a red card ban is likely to be less time- and resource-intensive than multi-year, direct engagement in the development, implementation, and monitoring of a bilateral VPA trade agreement. Whether the two mechanisms are equally likely to bring about desired governance reforms in the relevant sector (and, potentially, advance broader human rights, good governance, and development objectives more broadly) is something that should be closely studied in order to arrive at a well-informed comparative cost-benefit analysis of the two approaches.

Building the capacity of stakeholders

The EU's fostering and monitoring of multi-stakeholder VPA processes has been shown to open political space and empower civil society actors to help drive and design national reforms.²⁹ When the EU enters into dialogue with flag states under the IUU Regulation, it may resemble VPA negotiations in some ways, but the investigation, monitoring, and support required by the

²⁹ See *Improving Forest Governance: a comparison of FLEGT VPAs and their impact* (FERN, 2013), available at <http://www.fern.org/improvingforestgovernance>; *Do VPAs improve forest governance?* (FERN, 2016), available at <http://www.fern.org/impacts>

EU to conduct an IUU dialogue with flag states does not entail the same degree of investment as the negotiation of a trade agreement or the development and monitoring of a timber legality assurance system. This may mean that the IUU Regulation approach may not build the capacity of stakeholders to the same degree as FLEGT processes, which are squarely focused on fostering multi-stakeholder reform processes, including an emphasis on building the capacity of civil society to effectively engage in VPA processes.

Conclusions published from a joint meeting of the European Commission, national governments, industry and NGOs monitoring the IUU Regulation noted that ‘participants recognised the steps taken in some third countries towards collaborative engagement between government, NGOs, industry, and civil society to support enhanced fisheries management and control’ and that ‘there is a need for further efforts in this regard and continued information exchange between all stakeholders, in order to ensure that these activities are mutually reinforcing.’³⁰ The IUU Regulation takes into consideration the respective capacities of various flag states when assessing their compliance, and expressly provides for capacity building assistance.³¹ One delivery mechanism for this assistance is EU funds, the same mechanism used to fund NGOs to build the capacity of civil society organisations engaged in VPA processes. Further research is required to explore more precisely how such funding has been deployed and the degree to which this support has fostered multi-stakeholder reform processes.³²

If a carding system was explicitly geared towards ensuring the adoption and implementation of international principles and standards such those set out in UNDRIP or the VGGT, such a system would inherently point to building the capacity and respecting the rights of customary rights-holders by ensuring the implementation of standards such as Free, Prior, and Informed Consent (FPIC). In this way, such a system might do more to empower customary rights-holders than FLEGT has done, because these international standards themselves focus on securing customary tenure rights, including the procedural rights needed to deliver and secure customary tenure rights. In contrast, the ability of FLEGT to deliver meaningful reforms to secure and protect customary rights is more loosely vested in relatively vague promises of broader law reforms, implemented through multi-stakeholder processes.

2.3.2 Demand-side measures to segregate illegal products from the EU market: Catch certification scheme and IUU vessel list, compared to FLEGT licensing and EUTR due diligence

While the carding system aims to improve governance in the fish sector to reduce IUU fishing, the catch certification scheme and the IUU vessel list aim to segregate legal fish from illegal fish and allow only legally caught fish into the EU market. The purpose of both the catch certificate scheme and the IUU vessel list is similar to that of the EUTR and FLEGT licensing. However, the mechanics of these systems are very different. This section compares the EUTR’s due diligence requirements and the fish certification scheme, and argues that the due diligence approach is a better model for forest-risk commodities.

30 *Understanding the EU’s carding process to end illegal, unreported, and unregulated (IUU) fishing*, 6 October 2015 (main conclusions of the event published by Environmental Justice Foundation, Oceana, Pew Charitable Trusts, WWF), available at <http://www.iuuwatch.eu/2015/10/understanding-the-eus-carding-process-to-end-illegal-unreported-and-unregulated-iuu-fishing/>

31 Article 31(5)(d) and 31(7) of the EU IUU Regulation.

32 This might best be done through dialogue with NGOs engaged in monitoring implementation of the IUU Regulation, perhaps through a joint conference as suggested in section 5.

Reliance on government certification versus operator due diligence

The EUTR requires economic operators placing timber products on the EU market to exercise due diligence to assess and mitigate the risk that the timber was illegally harvested. EUTR due diligence entails a risk assessment of government documentation asserting that timber products are legal. Most official documentation is not considered to be absolute proof of legality. The only official documents that rise above this skepticism are FLEGT and CITES licenses.

By contrast, the IUU Regulation's catch certification scheme requires Member State competent authorities to rely on official documents from the flag state certifying the legality of fish caught by vessels operating under its flag. The only exception to this is if the EU, following investigation of and dialogue with the flag state, issues a red card. But the absence of a red card does not mean that a country's certification is necessarily robust and credible. This is expected to be different with FLEGT licenses. FLEGT licensing systems must be transparent and subject to extensive checks on the timber legality assurance system, including independent monitoring. The credibility of FLEGT licenses is based upon the stringency of these checks as well as the soundness of the traceability system and underlying legal framework. It will remain to be seen if FLEGT licenses will be perceived as credible.

There may be other reasons to choose to rely on operator due-diligence requirements rather than government certification schemes to manage and segregate sources of supply in line with criteria set out by EU regulations. In the case of forest-risk commodities, many of the major commodity trading companies have already made commitments to improve the traceability and sustainability of their supply chains by pledging to make them 'deforestation free'.³³ Implementing a government certification scheme – particularly one which assumes the credibility of producer countries' certification of legality in the absence of a robust monitoring system along the lines being developed through VPAs – seems to be a step in the wrong direction.

At the same time, companies that have pledged 'deforestation-free' supply chains are realising that it is very hard to deliver on these pledges without improved legal frameworks, transparency, governance, and law enforcement in producer countries. As suggested above, the IUU Regulation's carding system provides a possible alternative to a VPA-type approach for motivating governance improvements, including in relation to respecting customary tenure rights. It may be advisable, in the case of forest-risk commodities, to couple a carding system with an EUTR-type regulation imposing due-diligence obligations on private sector operators. This would reinforce the 'deforestation free' supply chain efforts already being developed by global commodity companies, rather than switching to government-issued supply chain verification along the lines of the IUU Regulation's catch certification scheme. Switching to a government-issued certificate would be more likely to displace or undercut, rather than reinforce, companies' current efforts to procure 'deforestation free' commodities. In contrast, a due diligence requirement imposed on companies could incorporate and reinforce existing efforts toward 'deforestation free' products into a drive for continual improvement to reduce to 'negligible' the risk that the products were cultivated on land that was illegally converted.

33 Duncan Brack et Al. *Agricultural Commodity Supply Chains: Trade, Consumption, and Deforestation* (Chatham House, January 2016); *Tracking Corporate Commitments to Deforestation-Free Supply Chains* (Supply Change, July 2016), available at http://www.illegal-logging.info/sites/files/chlogging/supply_change_forest_trends.pdf

Blacklisting rogue links in the supply chain

The IUU Regulation provides that vessels listed as having engaged in IUU fishing on the IUU vessel list are prohibited from docking at the ports of EU Member States and exporting their stocks into the EU market. If it were possible to apply a similar sanction to operators at various points in the supply chain for forest-risk commodities – to particular farms, mills, processors, or shippers found to routinely engage in illegal practices – this would provide a strong incentive for strict compliance because blacklisting would result in the operator being cut off entirely from the EU market. The IUU vessel list compiled by the European Commission is drawn from vessels listed as IUU by various RFMOs, which already have their own monitoring and enforcement systems. No similar monitoring and enforcement entities currently exist for forest-risk commodities. Therefore, if an official blacklist for operators in the supply chains for forest-risk commodities were developed, regulations would have to clearly set out the methods and criteria for blacklisting. NGOs could provide substantiated information that could help to provide the basis for such determinations. Companies working to achieve legal and/or deforestation-free supply chains might also have an interest in identifying and blacklisting supply chain operators working against these objectives.

2.3.3 Imposing sanctions on EU actors who benefit from illegal trade

The IUU Regulation's provisions for the prosecution and sanctioning of EU nationals and operators that finance or otherwise benefit from IUU fishing activities undertaken under the auspices of non-EU flag states provide a model for EU jurisdiction to cut off activities that would otherwise be outside its jurisdiction. The EU does not have jurisdiction to go after IUU activities undertaken under the flag of a non-EU state. However, the IUU Regulation provides for Member State competent authorities to prosecute EU nationals and operators that indirectly engage in these activities, whether by financing them or by operating surrogates in the flag state.

Fern has been looking at ways of tackling deforestation by ensuring that investors in agricultural production and trade of forest-risk commodities do not finance the conversion of forest land to large-scale agricultural production.³⁴ Others have focused on encouraging the voluntary and regulatory development of investment policies to assess and mitigate risks of investing in the conversion of forest land in violation of forest tenure rights and/or where high-value carbon stocks would be extinguished by the land conversion.³⁵ Incorporating the IUU Regulation's approach, the EU could adopt regulations to address deforestation that would require Member States to prosecute and sanction investors found to finance the illegal conversion of forest land. Such a measure would provide a direct threat to the individuals and companies financing deforestation and could provide a strong incentive and supplement to risk-based investment policies.

³⁴ Mark Gregory; *Financing landgrabs and deforestation; the role of EU banks and investors*; Fern 2016.

³⁵ See, e.g., *The Munden Project, The Financial Risks of Insecure Land Tenure* (Rights and Resources Initiative, December 2012), all available at <http://www.fern.org/financinglandgrabs>

3 Conflict minerals

In some developing countries the extraction, processing and trade of natural resources are not contributing to human development: instead they are financing armed groups which commit serious violations of human rights. The EU imports a significant amount of raw materials from regions affected by conflict. Sometimes these materials are imported in their raw form and processed in Europe. Other times, the materials are already processed or even incorporated into consumer products prior to being imported into the EU. In 2013, global imports of four ores that are most often used to fund conflicts in the south – tin, tantalum, tungsten, and gold ('3TG') – were worth over €123 billion and the EU accounted for about 16 per cent of this trade.

In response to global concern, the Organization for Economic Co-operation and Development (OECD) developed the OECD Due Diligence Guidance for Responsible Supply Chains and Minerals from Conflict-Affected and High-Risk Areas in May 2011.³⁶ The OECD guidance clarifies how companies can identify and better manage risks throughout the entire mineral supply chain, from miners, local exporters and mineral processors to the manufacturing and brand-name companies that use these minerals in their products. It has become the leading industry standard for companies looking to live up to the expectations of customers and of the international community on mineral supply chain transparency and integrity and has been endorsed by 34 OECD member countries, 19 other countries, and the UN Security Council.³⁷ It already forms the basis of laws in other countries including the US³⁸ and the Great Lakes Region of Africa, as well as guidance developed by the Chinese government for Chinese companies.³⁹

3.1 The proposed conflict minerals regulation

The European Commission proposed a draft *Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas* ('draft conflict minerals regulation').⁴⁰ The European Parliament proposed amendments to strengthen it in May 2015,⁴¹ and the European Council passed its mandate on the proposed regulation in December 2015.⁴² Following trilogue discussions that began in February 2016, the Commission, Parliament, and the European Council reached a 'political understanding' on a new EU regulation to address conflict minerals in June 2016⁴³ and called for further trilogue talks to agree the final text of the legislation.

36 See generally <http://www.oecd.org/corporate/mne/mining.htm>

37 *Ibid.*

38 US Dodd-Frank Wall Street Reform and Consumer Protection Act. For an assessment of the Dodd-Frank Act's provisions on conflict minerals, see *Digging for Transparency* (Amnesty International and Global Witness, April 2016), available at <https://www.globalwitness.org/en/campaigns/conflict-minerals/digging-transparency/>

39 For an NGO analysis of the Chinese guidance, see <https://www.globalwitness.org/en/press-releases/global-witness-welcomes-progressive-new-chinese-mineral-supply-chain-guidelines/>

40 Proposal for a *Regulation of the European Parliament and of the Council setting up a Union system for supply chain due diligence self-certification of responsible importers of tin, tantalum and tungsten, their ores, and gold originating in conflict-affected and high-risk areas*, COM (2014) 111 final.

41 See text published at <http://www.europarl.europa.eu/sides/getDoc.do?type=TA&language=EN&reference=P8-TA-2015-0204>. See also a joint NGO briefing summarizing and responding to the Parliament's amendments to the proposed conflict mineral regulation, *EU Regulation on Responsible Mineral Sourcing: Implementing the Parliament's Proposed Due Diligence System* (Amnesty International, Global Witness et al., October 2015), available at <https://www.globalwitness.org/en/campaigns/conflict-minerals/conflict-minerals-europe-brief/>

42 For an NGO response to the Council's mandate, see *EU Responsible Mineral Sourcing Regulation: Civil Society Response to the Council Mandate Agreed by Coreper* on 17 December 2015, available at <https://www.amnesty.org/en/documents/ior10/3415/2016/en/>

43 Conflict minerals: MEPs secure mandatory due diligence for importers (European Parliament News, June 2016), available at <http://www.europarl.europa.eu/news/en/news-room/20160615IPR32320/Conflict-minerals-MEPs-secure-mandatory-due-diligence-for-importers>; Political Understanding following the 15 June Trilogue on proposed conflict minerals regulation (MediaCentrum, June 2016), available at http://mediacentrum.groenlinks.nl/sites/default/files/political%20understanding%20conflict%20minerals%2015-06-2016_0.pdf

This paper highlights issues of concern in the various versions of the regulation that are also likely to come into play regarding any proposed legislation to regulate forest-risk commodities.

3.1.1 The European Commission's proposal

The Commission's proposed conflict minerals regulation set out a *voluntary* system for supply-chain due diligence under which importers of 3TG minerals and ores are invited to 'self-certify' as 'responsible importers' by declaring to the Member State competent authority that they comply with the following requirements:

- Provide documentation and information regarding the minerals and metals in line with the requirements set out in the OECD guidance on responsible sourcing of minerals;
- Comply with the OECD guidance standards (inter alia, prohibition on profiting from serious human rights abuses associated with mining operations, money laundering, bribery and tax-evasion, and supporting non-state armed groups directly or indirectly);
- Communicate to suppliers and the public their supply-chain policies for minerals and metals from conflict areas;
- Incorporate supply-chain policy engagements within contracts and agreements with suppliers;
- Create in their management structures responsibilities for the implementation and record-keeping of supply-chain due diligence;
- Assess risks of adverse impacts stemming from their supply chains (such as serious human rights abuses, bribery and money laundering operations) and address them in a risk-management plan to mitigate adverse impacts should they occur, and establish an early warning risk-awareness system.

Responsible importers would have to organise independent third-party audits verifying compliance with these requirements. Monitoring of the system would be undertaken by Member State competent authorities through ex-post checks where substantiated concerns have been raised.

Participation in the system proposed by the Commission would be voluntary and applicable only to upstream producers (smelters and refiners) and importers of 3TG.

3.1.2 European Parliament amendments to the proposed conflict minerals regulation

In May 2015 the European Parliament voted to strengthen the proposed regulation in two important ways. The Parliament called for **mandatory** due diligence and reporting by **EU operators by companies along the whole supply chain**.⁴⁴

Applying separate due diligence obligations to upstream and downstream operators

While emphasising the need to mandate due diligence along the entire supply chain, Parliament endorsed separate responsible sourcing obligations for two groups of companies: (1) EU-based

⁴⁴ Conflict minerals: MEPs ask for mandatory certification of EU importers (European Parliament News, May 2015), available at <http://www.europarl.europa.eu/news/en/news-room/20150513IPR55318/conflict-minerals-meps-ask-for-mandatory-certification-of-eu-importers>

importers of raw materials, which are located ‘upstream’ in the supply chain and (2) ‘downstream’ companies trading components and products that contain these minerals. ‘Upstream’ and ‘downstream’ links on 3TG supply chains are illustrated in **Figure 3**.

The Parliament’s text requires upstream companies such as metal processors, refiners, and mineral and metal traders who import 3TG ores, concentrates, and metals into the EU to carry out supply chain due diligence and publicly report on their efforts to do so. Article 4 requires companies to develop a company policy that sets out their commitments to responsible sourcing (a model policy is available in the OECD Guidance), and to put in place a chain of custody or traceability system that allows them to better understand their supply chains. Companies are expected to use the procedures developed through these policies and systems, and the information generated through their implementation, to identify risks and implement a strategy to address them (Article 5). Article 6 requires companies to carry out independent third-party audits of their due diligence practices. Article 7 requires companies to publicly report on the due diligence they are doing.

The obligations of downstream companies, such as manufacturers who first place products containing 3TG minerals on the European market, are set out in Amendment 155. This requires ‘first-placers’ to ‘take all reasonable steps to identify and address any risks arising in their supply chains for minerals and metals coming within the scope of this Regulation’, in accordance with the OECD guidance. They must also ‘provide information on the due diligence practices they employ for responsible supply chains.’

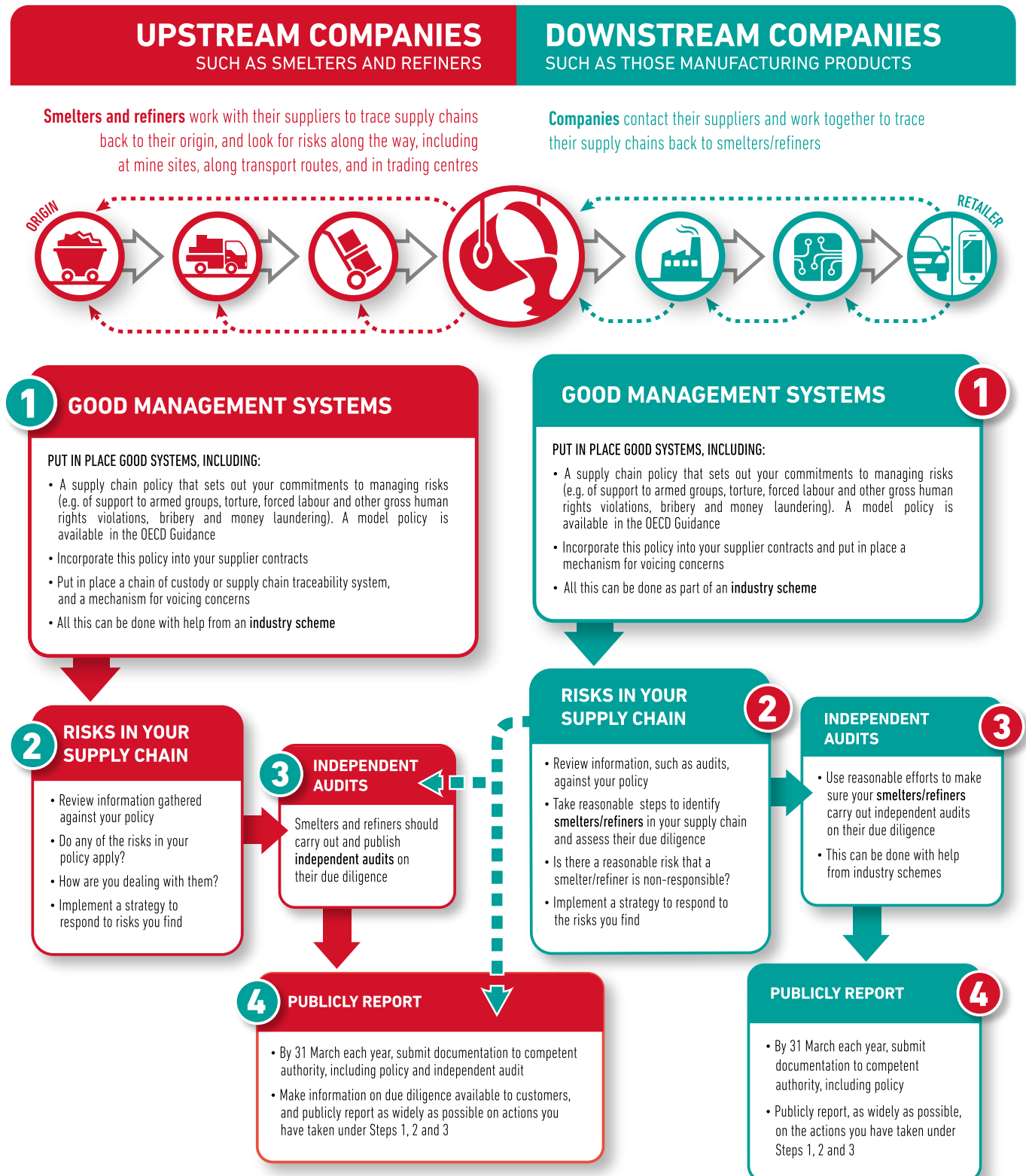
By including mandatory requirements for the whole supply chain, but differentiating between the obligations of downstream companies and those of companies closer to the source of the raw materials, the European Parliament’s Amendments better align the draft regulation with international standards by engaging the whole supply chain in the process. By aligning with the OECD Guidance, the Amendments also align the EU regulation with laws in other countries that also adhere to the OECD Guidance. Coherence across national regulatory frameworks in alignment with widely endorsed international standards makes it easier for companies operating globally to design systems that will comply with the demands of the many jurisdictions in which they do business. Parliament’s comprehensive supply chain coverage also would increase the effectiveness of the regulation in at least two other ways:

- It would tackle all the relevant trade flows, by covering not only imports of raw forms of 3TG, but also imports of 3TG contained within finished product (such as mobile phones, cars, and laptops), semi-finished products, and component parts.
- It would increase the regulation’s impact on supply chain practices globally. By including downstream ‘first placers’, the Parliament’s Amendments use EU commercial leverage to put pressure on other companies in the supply chain of EU companies, including the smelting community outside the EU. The Commission’s limited upstream approach misses this opportunity.

Bifurcating the supply chain helps overcome traceability challenges

Supply chains for 3TG minerals include the amalgamation and refinement of the ore followed by incorporation of relatively small amounts of metal as one component of complex consumer products. These complex global supply chains have clear ‘choke points’ at which the intermixing and refinement of raw material from multiple sources takes place. For 3TG, smelters/refiners are the choke point. As illustrated in **Figure 3**, both the upstream and downstream due diligence obligations for 3TG center around this choke point without requiring the traceability of specific

Figure 3: How Responsible Sourcing Works under the OECD Guidance and European Parliament Amendments to the European Commission's Proposed Conflict Minerals Regulation



consignments through the choke point. As discussed further in section 3.2.2, the supply chains for many forest-risk commodities entail similar complexity and revolve around clear choke points. Bifurcating due diligence for operators along forest-risk commodity supply chains in a similar fashion could help overcome objections that supply chain traceability is too burdensome.

Highlighting the flexible and progressive nature of due diligence

Parliament noted that '[t]he exercise of due diligence must be tailored to the activities of the undertaking in question, its size and its position in the supply chain' (Amendment 135) and asked the Commission to monitor and report on the impact of responsible sourcing on SMEs and to provide technical and financial assistance to SMEs (Amendment 10). In addition to highlighting the flexible nature of due diligence, Parliament also recognised that due diligence is a process of ongoing improvement (New Recital 9(a)).

The role of industry schemes

This emphasis on the nature of due diligence as striving for continual improvement is arguably undercut by Parliament's proposal that existing due diligence systems could be recognised as providing compliance with the EU conflict minerals regulation (Amendment 9). The adoption of the OECD Guidance as well as legislation to address conflict minerals in some countries has encouraged the development of many industry schemes, such as voluntary certification schemes, in recent years. Such schemes can help companies do their due diligence more effectively. However, as discussed further in section 3.2.1, when the EU expressly recognises certain schemes as providing compliance with a due diligence regulation, this can undermine the process of continual improvement by allowing an industry-regulated scheme to take the place of a company's individual responsibility to carry out and report on its due diligence. Where private schemes are recognised, limiting recognition only to schemes already in existence further discourages innovation and competition to develop more robust schemes to aid operators in their quest for continual improvement.

Defining a 'white list' of responsible smelters and refiners

While imposing mandatory due diligence obligations on downstream as well as upstream links in the supply chain, Parliament also sought to make this burden easier on downstream operators by maintaining the Commission's proposal to develop a 'white list' of responsible smelters and refiners (Article 8) and another white list of 'responsible importers' (Article 7(a)). This proposal suffers from the following weaknesses. First, the draft regulation does not set out any responsible sourcing criteria with which smelters/refiners (or importers) are required to comply in order to be on the white list. Also, as in the case of offering official approval to certain industry schemes, the official approval of certain operators through their inclusion on a white list endorsed by the EU arguably undermines the due diligence obligations the regulation assigns to operators. In particular, the ambition towards continual improvement inherent in due diligence can become compromised. Given the opportunity to tick a box by choosing a supplier already on an EU white list, an operator may no longer look for suppliers with higher standards and more transparent sourcing practices. It may stop requiring suppliers from the list to demonstrate their compliance with the OECD's responsible sourcing criteria for the consignments provided or to appropriately value these 'responsibility factors' when procuring bids for supplies.

Moreover, the draft regulation appears to employ a circular system for identifying which smelters, refiners, and importers are 'responsible'. Article 8 of the proposed regulation calls for the Commission to 'adopt and make publicly available a decision listing the names and addresses of responsible smelters and refiners of minerals within the scope of the regulation.' This list is to be



Child gold miners in Kaji, Democratic Republic of the Congo

ENOUGH Project - Lezhnev Flickr.com / CC

based on 'the information provided by the Member States in their reports as referred to in Article 15'. Article 15, in turn, requires Member States to submit to the Commission annual reports on the implementation of the Regulation, 'including any information on responsible importers as set out in Article 7(1) (a), 7.2 and 7.3(a) and (c)'. The portions of Article 7 cited in Article 15 call for self-certified responsible importers to identify 'responsible smelters or refiners in its supply chain'. Presumably, the list compiled and published by the Commission pursuant to Article 8 is intended to provide guidance to responsible importers as to which smelters and refiners can be considered 'responsible'. The contents of this list, however, are merely derived from lists of 'responsible smelters or refiners' identified to Member States by self-certified 'responsible importers'. Nowhere in the proposed regulation are the criteria and indicators that responsible importers – and their auditors – should use to determine which smelters and refiners can be classified as 'responsible'.

Accompanying supply-side measures to address governance challenges in producer countries

Parliament recognised the importance of taking a comprehensive approach to tackling the problems associated with conflict minerals by developing a set of supply-side measures to support governance reform and address other related development needs in producer countries. As an accompaniment to its draft conflict minerals regulation, the Commission and External Action Service issued a Joint Communication calling for building on political and raw material dialogues with third countries. Parliament took this a step further by requiring the Commission to submit a legislative proposal for accompanying measures aimed at engaging trading partner countries and building their capacity for improved governance in the minerals sector.

3.1.3 Council's mandate on the proposed conflict minerals regulation

The Parliament's Amendments were generally welcomed by the NGO community advocating for a strong conflict minerals regulation.⁴⁵ In contrast, the mandate adopted by the European Council in December 2015 was widely rebuked by NGO advocates.⁴⁶ These NGOs characterised the Council as aiming well below the ambition of the Parliament, and warned that the Council's position would 'significantly undermin[e] the leading international framework previously endorsed by the EU – the OECD's Due Diligence Guidance'.⁴⁷ Noting that many EU companies are already implementing the OECD due diligence framework in large part due to US legislation implementing the OECD Guidance, NGOs accused the Council mandate of 'watering down the meaning of being a responsible company'.^{48,49} By asking less of companies than the Guidance requires, the Council's mandate would present manufacturers and traders as 'responsible' even if they fail to comply with the OECD standard, thus striking a severe blow to the OECD Guidance and the international momentum gathering behind it. In addition, the mandate declined to impose any mandatory obligations on operators importing 3TG minerals or ores into the EU and failed to engage upstream operators at all through the regulation.

3.1.4 Trilogue Agreement

EU trilogue negotiations on the draft conflict minerals regulation began in February 2016 and resulted in a 'political understanding' between the Commission, the Parliament, and the Council in June 2016.⁵⁰ Key points of the agreement include:

- The OECD due diligence guidelines must serve as the overarching principle of the regulation and should be in no way undermined.
- With regard to recognition of due diligence schemes, both existing and future due diligence schemes can be recognised as providing compliance with the regulation's due diligence obligations, provided that such schemes are robust and aligned with the OECD Guidance. Criteria for recognition will be included in the regulation or as a package adopted by means of a delegated act and will be based on the OECD methodology.

45 See *EU Regulation on Responsible Mineral Sourcing: Implementing the Parliament's Proposed Due Diligence System* (Amnesty International, Global Witness, et al., October 2015), available at <https://www.globalwitness.org/en/campaigns/conflict-minerals/conflict-minerals-europe-brief/>

46 See *EU Responsible Mineral Sourcing Regulation: Civil Society Response to the Council Mandate Agreed by Coreper* on 17 December 2015, available at <https://www.amnesty.org/en/documents/ior10/3415/2016/en/>

47 *Ibid.* at 1 (noting that the OECD guidance had been negotiated and agreed by industry, governments, and civil society in 2009 and already forms the basis of laws in other countries, has been endorsed by 34 OECD member countries, 19 other countries, and the UN Security Council and forms the basis for Chinese industry standards on due diligence in mineral supply chains).

48 *Ibid.* at 1-2. See also *Digging for Transparency* (Amnesty International and Global Witness, April 2016) (assessing the US Dodd-Frank Act). The Dodd-Frank Act requires, among other things, US-listed companies to undertake due diligence to check if certain minerals in products are funding armed groups or fueling human rights abuses in Congo and its neighboring countries and to publicly disclose their due diligence efforts to the Security Exchange Commission in annual reports.

49 The Council's mandate proposes due diligence steps that fall well below the OECD standard: (1) The Council severely reduced the supply chain risk assessment expected of manufacturers and metal traders ('metal importers') by limiting the information these companies are expected to look at to 'available audits'. For example, companies would be permitted to leave out information in a company's possession (such as supplier policies and the information on the countries that smelters source from) or the public domain (such as UN and NGO reports). In other words, a company could comply with the regulation and thereby be considered 'responsible' even if it knows or has strong reasons to suspect that a smelter has behaved irresponsibly. (2) If a smelter audit is not available, the Council only expected metal importers to carry out ad hoc risk assessments. This is in contrast to the OECD Guidance, which makes clear that companies should put in place ongoing individual risk management processes so that they can respond to risks whenever and wherever they arise in their supply chain. (3) Making plain its disregard for the OECD Guidance, the Council removed references to the OECD Guidance as the due diligence standard that metal importers should meet. Not only does this strip the operators' obligation to assess or manage risk in accordance with any particular standard: it also leaves Member State competent authorities with no meaningful standard to assess operators' practices against.

50 *Conflict minerals: MEPs secure mandatory due diligence for importers* (European Parliament News, 16 June 2016), available at <http://www.europarl.europa.eu/news/en/news-room/20160615IPR32320/Conflict-minerals-MEPs-secure-mandatory-due-diligence-for-importers>; *Why the EU's New Deal on Responsible Mineral Sourcing is a Missed Opportunity* (Global Witness Blog, 11 July 2016), available at <https://www.globalwitness.org/fr/blog/why-eus-new-deal-responsible-mineral-sourcing-missed-opportunity/>

- The regulation will require mandatory due diligence for upstream importers of 3TG minerals, metals and ores, whose imports exceed a specified annual threshold.
- In relation to downstream operators, big EU firms that make or sell products containing 3TG will be encouraged to report on their sourcing practices based on a new set of performance indicators to be developed by the Commission, but they will not be subject to any mandatory requirements. These companies will be able to join a registry to be set up by the Commission and report voluntarily on their due diligence practices. In addition, the Commission shall review the functioning and effectiveness of the regulation, including an independent assessment of the proportion of downstream operators in the EU with 3TG in their supply chain that have voluntarily put due diligence systems in place. The review shall assess the adequacy, implementation, and impacts of these due diligence systems as well as the need for additional mandatory measures in order to ensure sufficient leverage of the total EU market on the responsible global supply chain of minerals.

Further trilogue negotiations are needed to hammer out the final text of the legislation before it is finally approved.

3.2 How components of the proposed conflict minerals regulations might translate to forest-risk commodities

The draft conflict minerals regulation – particularly the Parliament draft – offers important insights for demand-side regulation of forest-risk commodities to halt global deforestation. This section discusses the draft regulation’s key components and considers how these might be adapted to the context of forest-risk commodities.

3.2.1 Due diligence: A flexible, proactive approach to continual improvement

EU lawmakers have adopted both due diligence and certification approaches to segregate ‘good’ from ‘bad’ supply chains. The best outcomes can result when the two approaches are used synergistically.

The concept and practice of due diligence is well-defined and familiar to EU operators and regulators

Many EU companies and national authorities are familiar with the core principles of due diligence. The laws of the EU and Member States mandate due diligence in specific sectors, including the EU Anti-Money Laundering Directive and the EU Timber Regulation. While the concept can appear vague in comparison to ‘tick box’ criteria in certification standards, the contours of when a company’s due diligence systems and practices can be considered ‘reasonable,’ ‘adequate’ or ‘proportionate’ have been well developed in case law. This is because it is common practice to include due diligence as a defense in relation to alleged infractions of numerous regulations governing company behavior even where the regulation is not expressed in terms of placing due diligence obligations on companies. Accordingly, many EU and national authorities, in addition to the companies they regulate, are familiar with risk assessment and risk mitigation processes and systems in various contexts.

The draft conflict minerals regulation provides a recent example of EU lawmakers’ understanding of the feasibility, efficiency, and effectiveness of a due diligence approach and their willingness to impose due diligence obligations on EU operators in pursuit of sustainability objectives.

The importance of assigning responsibilities and liabilities

Tools such as voluntary certification schemes or other industry schemes can help companies to carry out their due diligence obligations. However, regulations should explicitly state that the responsibility to carry out and publicly report on due diligence rests with individual companies. Any assistance – whether in the form of white lists, black lists, industry schemes, or other tools – cannot release upstream or downstream operators from this individual obligation. In other words, membership in or compliance with a scheme should not, in itself, be equivalent to compliance with the regulation. Compliance tools should be viewed as providing assistance and evidence to support a company's exercise of due diligence, not substituting for it.

The OECD Due Diligence Guidance and other due diligence laws, including the EU Timber Regulation,⁵¹ make clear that companies must retain individual responsibility for their due diligence efforts and not pass that responsibility on to third parties. However, both the Parliament and the Council approach to the conflict minerals regulation are at odds with this principle.

A strong and effective regulation should be designed to exert maximum leverage to impact the problem it seeks to address in relation to the resources invested in its implementation and enforcement. One way to do this is to design regulations to 'activate' a wide range of stakeholders to develop the information and other elements necessary for the regulations' implementation. Such regulations will place clear legal responsibilities – and liabilities – on appropriate parties. Appropriately placed and well calibrated 'liability hooks' can, in turn, be expected to stimulate the cultivation, verification, dissemination, and appropriate use of relevant, credible information up and down the supply chain.

It is crucial that legal responsibilities and liabilities are clearly defined and maintained in any demand-led measures to reduce agricultural deforestation. The force of legal obligation and associated risk of penalty for breaches inevitably adds weight to the impact of a law and compels compliance. Legal leverage dissipates, however, where responsibility for ensuring compliance is shifted to another party, while the liability for compliance does not. The manner in which certification schemes can be used to prove compliance with biofuel criteria under the Renewable Energy Directive is a good example of this. The law allows for approved voluntary schemes to provide evidence of compliance with the criteria.⁵² However, in the event that biofuel feedstocks which do not, in fact, comply with the criteria are nevertheless certified by an approved scheme, neither the voluntary scheme nor the operator who relied on the scheme's faulty certification can be found liable or suffer consequences for this failure. This amounts to a 'liability loophole' rendering the regulatory scheme weaker than it would be if liability for such failures were clearly defined and enforced.⁵³

The use of voluntary schemes in the context of the EU Timber Regulation contrasts with how they are used for the Renewable Energy Directive's biofuels criteria. The EU Timber Regulation makes clear that ultimate legal responsibility for complying with its due diligence and prohibition

51 European Commission, *Guidance Document for the EU Timber Regulation*, C2016 755 final (Feb 2016), available at <http://documents.clientearth.org/wp-content/uploads/library/2016-02-12-guidance-document-for-the-eu-timber-regulation-ext-en.pdf>; Emily Unwin, *The EU Timber Regulation and the use of certification* (ClientEarth, March 2015), available at <http://documents.clientearth.org/wp-content/uploads/library/2015-03-16-the-eu-timber-regulation-and-the-use-of-certification-ce-en.pdf>; see also Emily Unwin, *Considering how the EU Timber Regulation may inform systems of governance for the sustainable production of commodities impacting forest ecosystems* (ClientEarth, Feb 2013), available at <http://www.documents.clientearth.org/library/download-info/considering-how-the-eu-timber-regulation-may-inform-systems-of-governance-for-the-sustainable-production-of-commodities-impacting-forest-ecosystems/>

52 Directive 2009/28/EC of the European Parliament and of the Council of 23 April 2009 on the promotion of the use of energy from renewable sources and amending and subsequently repealing Directives 2001/77/EC and 2003/30/EC

53 See *Biofuels – Driving best practice in voluntary certification* (ClientEarth 2013), available at <http://www.clientearth.org/reports/clientearth-driving-best-practice-in-voluntary-certification-may-2013.pdf>

requirements rests with operators (those that first place timber on the EU market). The EU Timber Regulation, and related secondary legislation and guidance, then sets out circumstances when certification schemes may be of use as tools for operators' exercise of due diligence. There is no obligation to use voluntary certification schemes; instead, each operator may decide whether or not to rely on voluntary certification schemes and, if so, which ones and in which circumstances. In any case, the operator will remain liable.⁵⁴ Maintaining liability for compliance with the regulation on operators ensures that liability loopholes will not emerge for the EU Timber Regulation through the use of certification as a compliance tool.

When utilised within a risk-assessment framework, quality certification schemes can provide a meaningful risk assessment tool. To ensure that 'liability hooks' are not displaced through reliance on certification, it is important that certification is well understood as a tool for compliance, and not simply equated with compliance. Avoiding the collapse of due diligence into certification schemes through the official approval of some certification schemes also maintains pressure on certification schemes to continually improve.

3.2.2 Alignment with widely-endorsed international norms and standards

A problem with framing EU legislation directed at global deforestation in terms of strict compliance with defined sustainability criteria is that there is no clear set of criteria pertaining to land use decision making that is articulated in comprehensive sustainability terms and which has been widely endorsed by governments internationally. Agreeing such criteria would be difficult, particularly as land use decisions often go to the very heart of national and regional and local economic development policy and given the inherent tension that exists between the economic, environmental, and social pillars of sustainability. While countries are generally willing to endorse the concept of sustainable development in general terms, how to balance the three pillars in any given situation is not something that any nation or community will easily give up to an international body or any other outside dictate.

As discussed in section 2.3.1, however, there is a substantial body of international law and other international agreements and norms relating to the rights of indigenous peoples, and customary tenure and use rights. Unlike the OECD Guidance, however, international agreements relevant to tenure and land use rights are not specifically framed in terms of due diligence.⁵⁵ So lawmakers would need to clarify the kinds of risks that due diligence aimed at reducing risk concerning the violation of tenure rights and how to recognise such risks. NGOs have begun to develop proposed principles, criteria and indicators for assessing land and resource tenure risks that can provide guidance to lawmakers and operators.⁵⁶ Three principles have been drawn from relevant international agreements:

1. Land use decisions must guarantee the Free, Prior, and Informed Consent (FPIC) of all potentially affected communities through the entire lifecycle of the project.
2. No conversion of contested land.

⁵⁴ See *Considering how the EU Timber Regulation may inform systems of governance for the sustainable production of commodities impacting forest ecosystems and Guidance Document for the EU Timber Regulation*, note 50 above.

⁵⁵ Measures requiring EU operators to exercise due diligence reduce the risk that commodities in their supply chains were cultivated on forest land converted to large-scale agriculture in violation of these international norms would be consistent with the use of due diligence provisions to secure international human rights in numerous other laws adopted in countries around the world. A 2012 study found over 100 due diligence provisions in the laws of 20 different countries, including in areas of law protecting human rights, such as labor laws and consumer protection. *Human Rights Due Diligence: The Role of States* (ICAR, December 2012).

⁵⁶ Anne van Schaik, Emily Unwin, Megan MacInnes, Reinier de Man, and Saskia Ozinga, *Discussion paper on proposed principles, criteria and indicators for assessing land and resource tenure risks for large-scale investment projects* (Friends of the Earth-Europe, ClientEarth, Global Witness, and Fern, unpublished, June 2015).

3. No violation of human rights in the acquisition or management of the land.

Building upon criteria and indicators from the most convincing existing systems, advocates have identified clear operational criteria and indicators for measuring compliance with these principles.⁵⁷

In addition to these principles drawn from international human rights law and the Voluntary Guidelines on the Governance of Tenure (VGGT), it makes sense to also posit legality as another principle to be respected. This means that other legal requirements relating to land-use decisions (and, especially, irreversible land-use change such as forest conversion) must also be observed. This might include requirements such as the need to prepare a social and environmental impact statement for a proposed land-use change.

3.2.3 Bifurcating supply chains around key choke points to address traceability challenges

Current supply chains for palm oil and other forest-risk commodities are not segregated nor easily traceable. Several companies that dominate international trade in forest-risk commodities have made 'zero deforestation' pledges and are making some progress in tracing and segregating supplies in line with this pledge.⁵⁸ The complexity of these supply chains makes traceability of particular consignments of a commodity from the farm to a product on a retail shelf challenging. This is due to the amalgamation of materials that happens during key processing choke points. This is particularly true for palm oil and soy, which are also, in turn, incorporated into a very wide range of end products.⁵⁹ Like minerals, global supply chains for palm oil have some clearly identifiable 'choke points' – namely, the mills at which the palm fruit or palm kernel is initially processed into oil and processing facilities further down the supply chain through which the oil is refined and then distributed for various applications and end products. See **Figure 4** for an illustration of palm oil global supply chains.

Bifurcating the supply chain around the choke point rather than expecting traceability through the choke points – as exemplified by the OECD Guidance and the proposed EU conflict minerals regulation – could provide a viable solution to the traceability dilemma. As in the conflict minerals regulation, separate due-diligence obligations could be imposed on upstream and downstream operators. Both would essentially focus on the choke points, but from a different angle. Imposing strict due diligence requirements on different parts of a bifurcated supply chain should be actively explored and would be preferable to other proposed solutions to the challenges of traceability in complex, global commodity supply chains, such as 'green palm' certificates.⁶⁰

3.2.4 Subjecting whitelisted companies to community monitoring

As discussed in section 3.1.2, there are some problems with the development of a white list of responsible suppliers as proposed in the draft conflict minerals regulation. The notion of a white list is nevertheless compelling. The provision of a white list would make the job of due diligence easier, and thus make it more likely that regulated companies might support the regulation. Moreover, it can be useful to be able to point to operators on a credible white list as examples of best practices towards which other suppliers should strive.

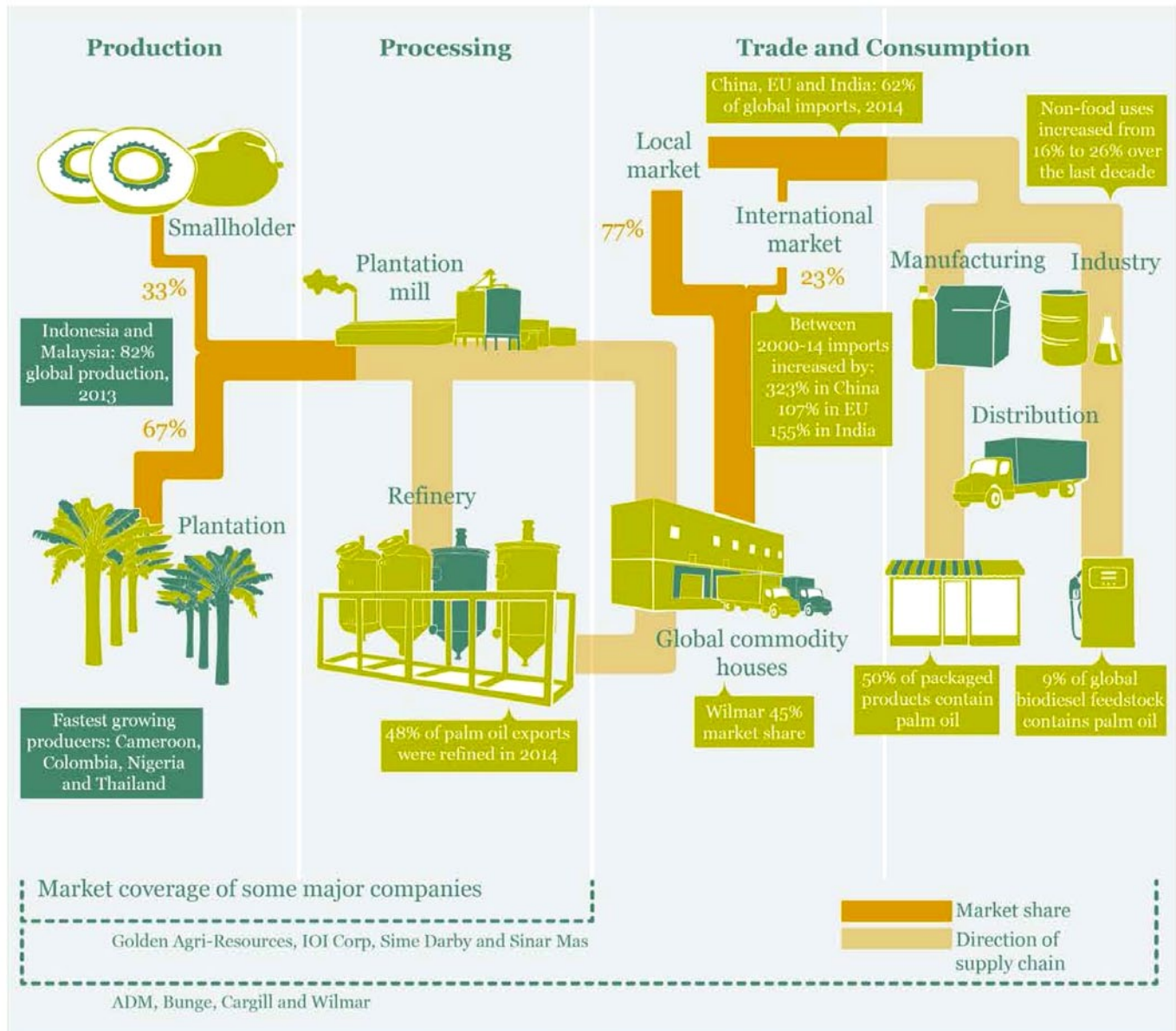
⁵⁷ *Ibid.*

⁵⁸ For an analysis of how these commitments are progressing, see *Supply Change: Corporations, Commodities, and Commitments that Count* (Forest Trends, March 2015); *Supply Change: Tracking Corporate Commitments to Deforestation-free Supply Chains* (Forest Trends, June 2016). See also *Responsible Sourcing: A Practical Guide* (Proforest, October 2015).

⁵⁹ For a further discussion of agricultural commodity supply chains, see Duncan Brack, Adelaide Glover and Laura Wellesley, *Agricultural Commodity Supply Chains: Trade, Consumption and Deforestation* (Chatham House, January 2016).

⁶⁰ See www.greenpalm.org

Figure 4: Global supply chains for palm oil



Reproduced from Duncan Brack, Adelaide Glover and Laura Wellesley, *Agricultural Commodity Supply Chains: Trade, Consumption and Deforestation* (Chatham House, January 2016).

One crucial component of best practice that should be included as a criterion for inclusion on a white list of responsible suppliers should be the willingness to be subjected to independent monitoring. In light of the issues at stake in land use and deforestation, it is crucial that operators in producer countries be subjected to community monitoring along the lines of that being developed in some VPA countries.

If a comprehensive framework to address a forest-risk commodity were developed to include both supply-side and demand-side measures, then the community monitoring of a white list could provide an important point of intersection between the demand- and supply-side components and engage the civil society and community organisations advocating governance improvements in producer countries to also engage with EU demand-side tools.

4 Recommendations for measures to address forest-risk commodities

This paper encourages focusing on international law and guidance pertaining to the rights of indigenous peoples and customary tenure and use rights as a reference for supply- and demand-side measures to address forest-risk commodities. The same measures could also advance the EU Action Plan on Human Rights and Democracy.

4.1 Supply-side measures

- Explore and consider proposing supply-side measures along the lines of the third-country carding process implemented in the IUU Regulation as a way to influence governance reforms in producer countries.
 - The principles and criteria for assessing whether a producer country should be issued a red or yellow card should be drawn from relevant international agreements focused on securing land and resource tenure rights, such as UNDRIP and the VGGT.
 - In addition, advocates should call for sufficient development assistance and other resources to be allocated to stakeholders in producer countries to support governance improvements, in particular to civil society organisations, indigenous peoples, and local communities.
- If measures to address forest-risk commodities includes the development of white lists comprised of suppliers deemed ‘responsible’ (or ‘legal’ or ‘sustainable’), advocates should insist that listed operators operating in producer countries should be subject to community monitoring, and inputs from community monitoring efforts should be taken into consideration in determining whether operators should remain whitelisted. The EU should also provide capacity building resources to develop and maintain effective community monitoring schemes.

4.2 Demand-side measures

- Encourage the development of a blacklisting tool such as the IUU vessel list. This list would be comprised of plantations, mills, refineries, shippers, and other operators along the supply chain known to routinely or systematically disregard community tenure and resource rights. Commodities coming through supply chains that include a blacklisted operator would be banned from the EU.
- Demand mandatory imposition of due diligence obligations on both upstream and downstream operators in forest-risk commodity supply chains. For supply chains that typically include key choke points at which supplies from numerous and varied sources are amalgamated in the course of processing and refinement, separate due diligence obligations could apply to upstream and downstream operators – as in the OECD Guidance and Parliament’s Amendments to the Commission’s proposed conflict minerals regulation. This could help to overcome the problem of tracing supplies through the choke points.
- Ensure that due diligence remains the responsibility of economic operators trading in forest-risk commodities (and products that incorporate these commodities) and are not displaced onto voluntary certification schemes or other third parties. In this way, the measures will

avoid providing a 'liability loophole' and ensure that the due diligence obligations incentivise continual improvement.

- Propose regulations that would require Member State competent authorities to investigate and prosecute EU nationals or EU-based companies that benefit from illegal land conversion in producer countries by financing or operating surrogate companies in third countries, along the lines of provisions in the IUU Regulation.

5 Proposed next steps

Several of the recommendations made in this paper require further research and elaboration before they can be taken forward. Hence the following measures are required.

5.1 Convene NGOs working in fishing, minerals, and forest sectors to share lessons

To fully assess the operation and effectiveness of the IUU fishing and conflict minerals regulations examined in this paper, as well as whether they could be effectively adapted to forest-risk commodities, it is also necessary to examine more closely how the measures are being implemented on the ground, the challenges encountered, and successes achieved. Prior to engaging in a campaign aiming for the adoption of similar measures to address forest-risk commodities, it would also be wise to learn more about the political battles waged by NGOs active in the development of the regulations sought to be replicated or adapted for forest-risk commodities – battles lost as well as battles won. This enquiry should include the identification of key champions as well as key opponents in the European Commission, European Parliament, and Member States.

This paper has relied primarily on desk research, which is generally not well-tailored to gain detailed insights into these questions. To pursue these questions, Fern should consider as a next step convening a conference including the key NGOs involved in the IUU Regulation, the FLEGT Action Plan, the proposed EU conflict minerals regulation, and those interested in advancing EU measures to address forest-risk commodities. Fern might also consider including NGOs monitoring the garment sector because, like efforts to address forest-risk commodities, the EU Responsible Garment Supply Chain Platform is at a relatively early stage.

5.2 Research how the key principles in relevant international agreements aimed to protect forest tenure can be understood and articulated to frame a risk-based due-diligence system

This paper recommends that international law and guidance pertaining to human rights, the rights of indigenous peoples, and customary tenure and use rights be referenced as the basis for due diligence obligations imposed on supply chain operators for forest-risk commodities. Further work is required to translate the key rights and principles articulated in these international laws and guidance documents into a risk-assessment and risk-mitigation framework that could be utilised by operators exercising due diligence.

5.3 Urge parties to other relevant international agreements to pursue international guidelines defining a due diligence framework for ‘deforestation free’ palm oil, soy, and other forest-risk commodities

Halting the conversion of forest land to large-scale agriculture is relevant to the Sustainable Development Goals, the 2014 New York Declaration on Forests, and the UNFCCC Paris Agreement. However, none of these agreements sets out specific terms and conditions for assessing whether palm oil, soy, or other forest-risk commodities were derived from converted forest land. Research into dialogues and other next steps being undertaken by the parties to these agreements should

explore whether the parties might try to develop an international set of due diligence norms and standards to help economic operators assess and mitigate the risk that the commodities it sources are derived from converted forest land. These could be developed along the lines of the OECD Guidelines for conflict minerals. Widely endorsed international guidelines could then, in turn, form the basis for EU demand-side regulations, just as the OECD guidelines have been incorporated into the EU's draft conflict minerals regulation as well as US legislation and Chinese guidelines for Chinese overseas investors.

5.4 Research into the criteria and process of defining and monitoring 'white lists' and 'black lists' of good and bad supply chain operators

This paper draws on the example of a black list authorised by the IUU regulation and recommends the compilation of official black lists of rogue supply chain operators that routinely or blatantly trade in forest-risk commodities derived from land converted in violation of human rights, indigenous peoples' rights, and customary tenure and use rights. In the IUU example, the IUU vessel list is comprised of vessels included in IUU vessel lists compiled by various Regional Fisheries Monitoring Organizations (RFMOs), and enforced by banning listed vessels from docking and unloading at Member State ports. The development and utilisation of a black list for operators at various points in the supply chains for forest risk operators would be more difficult to compile and enforce, however. Further research and discussion is required to detail the criteria and process for defining and enforcing black lists for forest-risk commodities supply chain operators.

Likewise, this paper draws on the example of white lists authorised in the draft conflict minerals regulation and recommends the compilation of official white lists of supply chain operators that exemplify best practices as a tool to aid companies in fulfilling due diligence obligations proposed for forest-risk commodities. The process and criteria for compiling the white lists of 'responsible suppliers' under the draft conflict minerals is flawed, however, because it relies on the unchecked self-selection of companies for inclusion on the white list. Further research and discussion is required to detail the criteria and process for defining and monitoring white lists for forest-risk commodities supply chain operators.

5.5 Develop alliances with NGOs monitoring the implementation of the EU Action Plan on Human Rights and Democracy

Objective 17 of the Human Rights Action Plan calls on the EU to foster a comprehensive agenda to promote Economic, Social, and Cultural Rights (ESCR) including 'land-related human rights issues, and indigenous peoples, in the context of *inter alia* "land grabbing" and climate change'. Objective 18 calls on the EU to advance business and human rights through 'a strong focus on business and human rights in the overall EU strategy on Corporate Social Responsibility including priorities for the effective implementation of the UN Guiding Principles on Business and Human Rights (UNGPs)', including the development and implementation of National Action Plans (NAPs) on the implementation of the UNGPs in national corporate social responsibility Strategies and the sharing of experiences and best practices in developing NAPs. Objective 25 is directed towards the EU's trade and investment policy and calls for the EU to, among other things, analyse the human rights impacts of trade and investment agreements. The EU's implementation of its Human Rights Action Plan is due to be reviewed in 2017.



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