

<b>Title:</b> <b>FLEGT (Forest Law Enforcement Governance and Trade) licensing scheme, implementing FLEGT Regulation 2005</b>  <b>Lead department or agency:</b> Defra <b>Other departments or agencies:</b>	<b>Impact Assessment (IA)</b>
	<b>IA No:</b> DEFRA0171
	<b>Date:</b> 20/05/2011
	<b>Stage:</b> Final
	<b>Source of intervention:</b> EU
	<b>Type of measure:</b> Secondary legislation
<b>Contact for enquiries:</b> Nicola Sale International Forestry Team	

## Summary: Intervention and Options

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

Illegal logging, alongside slash-and-burn agriculture, industrial commodity production, mining and infrastructure development are major drivers of global tropical deforestation. Deforestation, and the overexploitation of forest ecosystems globally, pose serious challenges to the international community. Global deforestation, which constitutes annual losses of forest areas the size of England has significant negative impacts. The TEEB study estimated the value of the ecosystem services lost as a result of deforestation at \$2tr-\$4.5tr each year, these losses are felt local both locally by the rural poor in developing countries and globally through the link to climate change and biodiversity loss. Further, illegal logging results in revenue losses to governments and legitimate businesses.

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

The FLEGT Regulation aims to change the behaviour of European timber and timber product importers by requiring them to alter their mechanisms for sourcing timber products from international suppliers, creating demand for legally verified (FLEGT) timber, and thereby also providing assurance to voluntary partnership agreement (VPA) countries that their efforts in implementing the licensing system will not place them at a competitive disadvantage with non-VPA countries. This will have broader benefits in terms of tackling illegal logging, and avoiding the serious economic, environmental and social problems of deforestation at the global scale.

### What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Five options were considered at the FLEGT Regulation negotiation stage: i.) Oppose the Proposed FLEGT Regulation and 'Do nothing'; ii.) Oppose the proposed Regulation and introduce a multi-lateral agreement; iii.) Oppose the proposed Regulation and introduce a ban on illegal timber; iv.) Accept the proposed Regulation; v.) Seek amendments to the proposed Regulation. Options i-iii are now not possible because the UK has agreed the FLEGT Regulation, indeed the UK was a key supporter of legislation at the negotiation stage. Due to the serious problems caused by illegal logging, we supported the Commission in driving forward the FLEGT Regulation in 2005, as well as further initiatives to support governance reform in key forest nations, and therefore our chosen option is to implement the Regulation. We will be taking option iv) and accepting the proposed regulation.

**Will the policy be reviewed?** It will be reviewed. **If applicable, set review date:** 9/2014

**What is the basis for this review?** Not applicable. **If applicable, set sunset clause date:** Month/Year

**Are there arrangements in place that will allow a systematic collection of monitoring information for future policy review?**

Yes

**SELECT SIGNATORY Sign-off** For final proposal stage Impact Assessments:

*I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.*

Signed by the responsible SELECT SIGNATORY: \_\_\_\_\_ Date: \_\_\_\_\_

# Summary: Analysis and Evidence

# Policy Option 1

## Description:

Option (iv)

Price Base Year 2009	PV Base Year 2011	Time Period Years 7	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	High: Optional	Best Estimate: - £7.8m

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low		£615k	£3.8m
High		£1950k	£11.9m
Best Estimate		£1280k	£7.8m

### Description and scale of key monetised costs by 'main affected groups'

Costs are presented as they will be faced by business, in this case UK importers who import timber and timber products from current (Ghana, and Republic of Congo,) and future countries which sign a Voluntary Partnership Agreement (VPA) with the EU, to verify the legality of their timber exports. These include charges aimed at full cost recovery for the Government to cover the costs of checking and verifying shipments. Costs are expected to be low as a proportion of shipment values (<1%).

### Other key non-monetised costs by 'main affected groups'

Nil

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low			
High			
Best Estimate			

### Description and scale of key monetised benefits by 'main affected groups'

No benefits could be monetised; some benefits fall outside of the UK.

### Other key non-monetised benefits by 'main affected groups'

International: difficult to disaggregate UK's impact as a proportion of the changes driven by FLEGT, but benefits accrue to VPA countries in terms of reduced losses in avoided taxes and benefits to legal operators, governance reform, forest sector reform, avoided corruption, avoided loss of livelihoods, avoided deforestation, avoided greenhouse gas emissions and avoided biodiversity. Domestic: Access to certified legal timber for UK suppliers and manufactures and associated market value.

### Key assumptions/sensitivities/risks

Discount rate (%) 3.5%

Assumption that further VPAs will be signed which will increase the workload for checking FLEGT licensed shipments; a key factor in the cost effectiveness of the Government's charging scheme, and would be expected to keep costs low. If no further VPAs come on board, the charge might never become relevant, and costs to importers reduced accordingly.

Direct impact on business (Equivalent Annual) £m):			In scope of OIOO?	Measure qualifies as
Costs: £1.28m	Benefits:	Net: - £1.28m	No	NA

## Enforcement, Implementation and Wider Impacts

What is the geographic coverage of the policy/option?		United Kingdom			
From what date will the policy be implemented?		01/09/2011			
Which organisation(s) will enforce the policy?		AH,UKBA and HMRC			
What is the annual change in enforcement cost (£m)?		Minimal			
Does enforcement comply with Hampton principles?		Yes			
Does implementation go beyond minimum EU requirements?		No			
What is the CO <sub>2</sub> equivalent change in greenhouse gas emissions? (Million tonnes CO <sub>2</sub> equivalent)		Traded:		Non-traded:	
Does the proposal have an impact on competition?		No			
What proportion (%) of Total PV costs/benefits is directly attributable to primary legislation, if applicable?		Costs:		Benefits:	
Distribution of annual cost (%) by organisation size (excl. Transition) (Constant Price)	Micro	< 20	Small	Medium	Large
Are any of these organisations exempt?	No	No	No	No	No

## Specific Impact Tests: Checklist

Set out in the table below where information on any SITs undertaken as part of the analysis of the policy options can be found in the evidence base. For guidance on how to complete each test, double-click on the link for the guidance provided by the relevant department.

Please note this checklist is not intended to list each and every statutory consideration that departments should take into account when deciding which policy option to follow. It is the responsibility of departments to make sure that their duties are complied with.

Does your policy option/proposal have an impact on...?	Impact	Page ref within IA
<b>Statutory equality duties<sup>1</sup></b> <a href="#">Statutory Equality Duties Impact Test guidance</a>	Yes	18
<b>Economic impacts</b>		
Competition <a href="#">Competition Assessment Impact Test guidance</a>	Yes	17
Small firms <a href="#">Small Firms Impact Test guidance</a>	Yes	17
<b>Environmental impacts</b>		
Greenhouse gas assessment <a href="#">Greenhouse Gas Assessment Impact Test guidance</a>	Yes	18
Wider environmental issues <a href="#">Wider Environmental Issues Impact Test guidance</a>	Yes	18
<b>Social impacts</b>		
Health and well-being <a href="#">Health and Well-being Impact Test guidance</a>	Yes	18
Human rights <a href="#">Human Rights Impact Test guidance</a>	Yes	18
Justice system <a href="#">Justice Impact Test guidance</a>	Yes	18
Rural proofing <a href="#">Rural Proofing Impact Test guidance</a>	Yes	18
<b>Sustainable development</b> <a href="#">Sustainable Development Impact Test guidance</a>	Yes	18

<sup>1</sup> Public bodies including Whitehall departments are required to consider the impact of their policies and measures on race, disability and gender. It is intended to extend this consideration requirement under the Equality Act 2010 to cover age, sexual orientation, religion or belief and gender reassignment from April 2011 (to Great Britain only). The Toolkit provides advice on statutory equality duties for public authorities with a remit in Northern Ireland.

## Evidence Base (for summary sheets) – Notes

Use this space to set out the relevant references, evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Please fill in **References** section.

### References

Include the links to relevant legislation and publications, such as public impact assessments of earlier stages (e.g. Consultation, Final, Enactment) and those of the matching IN or OUTs measures.

No.	Legislation or publication
1	
2	
3	
4	

+ Add another row

### Evidence Base

Ensure that the information in this section provides clear evidence of the information provided in the summary pages of this form (recommended maximum of 30 pages). Complete the **Annual profile of monetised costs and benefits** (transition and recurring) below over the life of the preferred policy (use the spreadsheet attached if the period is longer than 10 years).

The spreadsheet also contains an emission changes table that you will need to fill in if your measure has an impact on greenhouse gas emissions.

#### Annual profile of monetised costs and benefits\* - (£m) constant prices

	Y <sub>0</sub>	Y <sub>1</sub>	Y <sub>2</sub>	Y <sub>3</sub>	Y <sub>4</sub>	Y <sub>5</sub>	Y <sub>6</sub>	Y <sub>7</sub>	Y <sub>8</sub>	Y <sub>9</sub>
<b>Transition costs</b>										
<b>Annual recurring cost</b>										
<b>Total annual costs</b>										
<b>Transition benefits</b>										
<b>Annual recurring benefits</b>										
<b>Total annual benefits</b>										

\* For non-monetised benefits please see summary pages and main evidence base section



Microsoft Office  
Excel Worksheet

## Evidence Base (for summary sheets)

There is discretion for departments and regulators as to how to set out the evidence base. However, it is desirable that the following points are covered:

### 1. Introduction and Background

#### Problem under consideration;

1.1. Illegal logging, alongside slash-and-burn agriculture, industrial commodity production, mining and infrastructure development are major drivers of global tropical deforestation<sup>1</sup>. Deforestation, and the overexploitation of forest ecosystems globally, pose serious challenges to the international community. Global deforestation, at a rate of 13 million hectares every year, which constitutes the annual loss of an area the size of England<sup>2</sup>, causes enormous environmental and other damage, for example threatening:

- the livelihoods of over 90% of the 1.4 billion people globally who currently live in extreme poverty<sup>3</sup>;
- about 80% of the world's remaining terrestrial biodiversity, representing a catastrophic effect on global biodiversity, which itself has further detrimental impacts on human welfare, livelihoods and resource availability<sup>4</sup>;
- the stability of the global climate – deforestation, globally, is the source of approximately 18% of anthropogenic greenhouse gas emissions which lead to climate change, greater than those of the entire transport sector worldwide, with a number of feedbacks in the Earth's climate system which drive further emissions<sup>5</sup>;
- 10 million jobs provided by the forest products industry, and perhaps 50 million in the informal forest products sectors.

1.2. Illegal logging, and the damaging deforestation that it drives are serious issues to the global community. The UK government has a longstanding commitment to tackling illegal logging. Illegal logging can include a number of illegal activities, such as the harvest, transportation, purchase or sale of timber in violation of laws in the countries where it occurs.

1.3. Illegal logging undercuts the competitiveness of legitimate forest industry operations in exporting and importing countries. The World Bank<sup>6</sup> estimates that US\$5 billion (roughly GBP£3-4billion) per year is lost by Governments globally because of uncollected taxes and royalties on timber harvests (both those which are legally sanctioned, and those of which authorities are not aware), in addition to US\$10 billion (GBP£6-8 billion) globally through lost assets and revenue. Illegal logging also threatens the wellbeing of people who depend on forests for their livelihoods, and biodiversity as described above.

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<sup>1</sup> Butler, R.A. and Laurance, W.F., New strategies for conserving tropical forests Trends in Ecology & Evolution, Volume 23, Issue 9, September 2008, Pages 469-472

<sup>2</sup> Mitchell, A. *et al.* 2008. Forests NOW in the Fight against Climate Change; Forest Foresight Report 1.v3. Global Canopy Programme, Oxford, p10]

<sup>3</sup> <http://www.globalcanopy.org/main.php?m=120>

<sup>4</sup> <http://www.grida.no/publications/vg/forest/page/3795.aspx>

<sup>5</sup> Ibid, (Global Canopy Programme *forest foresight report 1 v3* Nov 2008) p5

<sup>6</sup> [http://siteresources.worldbank.org/INTFORESTS/Resources/ForestLawFINAL\\_HI\\_RES\\_9\\_27\\_06\\_FINAL\\_web.pdf](http://siteresources.worldbank.org/INTFORESTS/Resources/ForestLawFINAL_HI_RES_9_27_06_FINAL_web.pdf)

## **Rationale for intervention;**

- Deforestation occurs for a range of reasons linked to market failures and poor governance. The failure of domestic and international markets to value environmental benefits is the most pervasive market failure. Ineffective regulation and corrupt practices lead to capture by elites of the benefits that forests provide. Inequitable access to forests undermines local livelihoods. More than half of the world's tropical forests are locations of on-going or recent conflicts.
- The causes of the problem of illegal logging are complex, but can be attributed broadly to failure of international markets, which continue to accept illegal timber products, and failures of governance which allow commercial and political elites to benefit from forest exploitation by evading national forest laws in producer countries. Consumer countries have a key role in putting in place policies to control the flow of illegal timber into the European Union. The range of activities undertaken by the EU to target this complex problem is captured in the Forest Law Enforcement Governance and Trade (FLEGT) Action Plan, 2003<sup>7</sup>.
- Any attempt to exclude illegal timber products from international markets runs into the problem that it is generally impossible to distinguish legal from illegal products at the border. The intention of the FLEGT Regulation is that FLEGT-licensed timber products will be considered to have been legally harvested. As a result, such timber will not require any further legality assurance, thus stimulating the market for FLEGT timber, and thereby also providing assurance to VPA countries that their efforts in implementing the licensing scheme will not place them at a competitive disadvantage with non-VPA countries.

## **Policy objective;**

- The main objective of the FLEGT Licensing Regulation and Implementing Regulation is to establish the structures necessary to implement EU policies to target illegal logging and the consequent trade in timber and timber products, and thereby tackle one of the major drivers of deforestation.
- The FLEGT Regulation aims to change the behaviour of European operators by requiring them to alter their mechanisms for sourcing timber products from international suppliers. They will need to satisfy themselves that shipments will arrive at the UK border with a valid FLEGT licence, thereby ensuring that the timber and timber products they sell have been legally harvested. Timber will be monitored from FLEGT VPA countries, to ensure that the FLEGT licence, essentially a declaration of legality by the VPA country, accompanies all shipments.

## **Description of options considered (including do nothing);**

- As indicated in the introductory section above, the primary benefits of reduced illegal logging will fall predominantly outside UK borders, so the FLEGT licensing scheme needs to be seen in this context of wider development, environment and climate change policy. Secondary benefits in terms of nature conservation and climate change mitigation are global benefits.
- It is clear that eliminating illegal logging will also help nations avoid major losses of government revenue. A number of studies have estimated the cost of illegal logging to forests nations. The World Bank estimates costs of illegal logging at \$15 billion per year reporting that "where illegal logging in public lands alone causes estimated losses in assets and revenue in excess of US\$10 billion annually" and that "As much as US\$5 billion is lost

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<sup>7</sup> <http://ec.europa.eu/environment/forests/flegt.htm>

annually to governments because of evaded taxes and royalties on legally sanctioned logging”<sup>8</sup>. Forestry contributes about 10% of GDP in 19 African countries, as well as roughly 10% of trade in ten African countries.

- The FLEGT licensing scheme will involve a small (approximately £15.8k p.a. in the first year - see 2.9 for detail on how this was estimated) additional administrative burden per annum for industry and Government, given that it will build on existing systems used for implementing the European Wildlife Trade Regulations<sup>9</sup>, and the Convention on International Trade in Endangered Species of Flora and Fauna (CITES)<sup>10</sup>, as well as building on good practice in the industry across the EU on working with suppliers to raise legality standards in the procurement of timber and timber products. UK industry is recognised as a leader in the area of developing supply chain management and legality verification systems.
- Five options were considered at the FLEGT Regulation negotiation stage at the end of 2005: i.) Oppose the Proposed FLEGT Regulation and ‘Do nothing’; ii.) Oppose the proposed Regulation and introduce a multi-lateral agreement; iii.) Oppose the proposed Regulation and introduce a ban on illegal timber; iv.) Accept the proposed Regulation; v.) Seek amendments to the proposed Regulation. Options i.)-iii.) are now not possible because the UK has agreed the FLEGT Regulation at the European level, indeed the UK was a key supporter of legislation at the negotiation stage. We are in parallel supportive of the European Commission's proposed Regulation setting out the responsibilities of all operators placing timber on the European Community market
- Due to the serious problems caused by illegal logging, we supported the Commission in driving forward the FLEGT Regulation in 2005, as well as further initiatives to support governance reform in key forest nations. We therefore supported option v.) above; given we supported the Regulation although made some amendments to the text during the negotiation. We are now implementing this (amended) regulation.

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

1.4. We intend to include a provision requiring periodic biennial evaluations of the operation of the FLEGT licensing scheme in UK legislation putting the scheme into effect. Article 9 of the FLEGT Regulation also includes provision for reporting and proposals for improvement, where appropriate, 2 years after the first VPA is added to Annex two of schedule. Evaluation and monitoring will therefore also be undertaken at the European level. We will endeavour to input into these evaluation exercises and run our own evaluations in parallel.

## **2. Benefits and Costs**

### **Costs accruing to the UK Government**

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<sup>8</sup> [http://siteresources.worldbank.org/INTFORESTS/Resources/ForestLawFINAL\\_HI\\_RES\\_9\\_27\\_06\\_FINAL\\_web.pdf](http://siteresources.worldbank.org/INTFORESTS/Resources/ForestLawFINAL_HI_RES_9_27_06_FINAL_web.pdf)

<sup>9</sup> The ‘European Union Wildlife Trade Regulations’ is a term used in respect of a number of Regulations which implement CITES, and covers: Council Regulation (EC) No. 338/97; Commission Regulation (EC) No. 865/2006 and Commission Regulation (EC) No 811/2008

<sup>10</sup> <http://www.defra.gov.uk/animalhealth/cites/> The Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES) is an international agreement between governments that came into force in 1975. Its purpose is to ensure that no species of wild fauna or flora becomes or remains subject to unsustainable exploitation because of international trade. CITES accords varying degrees of protection to over 30,000 species of animals and plants, whether they are traded as live or dead specimens, parts (such as ivory or leather), or derivatives (such as medicines made from animals or plants). The member countries act together by regulating trade in species listed under the three appendices to the CITES Convention.

- 2.1. There will be ongoing costs to Government associated with the checks, administration, verification of legality of the licence, and communications with HMRC clearance processes, as well as one-off costs of additional information technologies, communications systems and administrators needed to run and update current systems in the Competent Authority. We currently propose to recover these costs, both one-off and running costs through a full cost recovery model. These costs are incorporated in to the Government's initial estimate of the charge to be applied to each shipment from year three onwards, which we have summarised at Table 2.
- 2.2. These costs are accrued through a fee to be charged to businesses at the onset of a charging regime from year three onwards, and thereby represent the cost to Government of running the FLEGT licensing scheme. This fee reflects the estimated total cost to the UK Government of checking, processing and investigating (where necessary, a number of) FLEGT licences.
- 2.3. There will also be other costs associated with training UK CITES Licensing Management Authority, UK Border Agency and HM Revenue and Customs officers in these new responsibilities, prosecuting those guilty of an offence associated with failure to present a valid FLEGT licence, running auctions for seized shipments, and other elements of running the scheme, and we will be working with the Competent Authority, the UK Border Agency, HM Revenue and Customs and the Ministry of Justice to develop options for funding these elements and minimising additional expenditure. Under this regulation we propose that those acting illegally (i.e bringing timber into the EU without a valid FLEGT licence) will be expected to bear the costs associated with detention of the timber, and if applicable costs associated with restoration, donation or destruction of seized timber.

#### **Costs accruing to importers of FLEGT licensed timber shipments**

- 2.4. The European Commission estimated in its own Impact Assessment that the costs to industry of implementing the FLEGT licensing scheme are proportionate to the need for the European Community to improve the efficiency of its policies against illegal logging and the related trade. The approach means that over time, UK, and other European, operators will benefit from the elimination of illegal timber products from the market, and therefore be increasingly confident in the legality of production of the raw materials in their supply chains.
- 2.5. We propose that there will be no charge for years one and two of the FLEGT licensing scheme, but that a charge be revisited, and perhaps imposed from year three onwards. The licence charge which might be incorporated from year three, has been estimated to cover the total sum of the full cost to Government of checking and verifying FLEGT licences over the first seven years of operation, on a working assumption of increasing flows of FLEGT timber to the UK (based upon further VPAs having been signed). NB. We further explain the rationale behind this licence charge, which is the result of a Full Cost Recovery model below.
- 2.6. The table below illustrates how a delayed Full Cost Recovery model might work, starting from year three onwards. Charging operators from year three onwards, when we expect an increasing number of shipments will arrive in the UK, enables the UK Government to recoup its own running costs. The table demonstrates how an estimated number of shipments, when multiplied by an initial estimation of this possible charge for checking each licence, results in Full Cost Recovery. The Government's estimate of its running costs has been produced by taking into account a Government administrator's time to check the licence for its completeness and validity, data input time to communicate receipt of this licence to the UK border authorities, and an intelligence-led investigations regime (which is described in section 9 of the consultation document). Costs would remain under periodic review, and are presented for the first 7 years



over which full cost recovery would be anticipated. Given uncertainties over how VPAs may develop going forward no new agreements are assumed after year 5.

2.7. Table 1, provides an estimate of the number of shipments of timber that could come from VPA countries based upon both evidence of past import volumes and values included in the previous consultation IA on FLEGT, as well as updated projections based on the number of shipments in 2009/10. As the updated figures on 2009/10 shipments exceed the previous forecasts, we have provided a range of estimates for costs based on either constant shipments at 2009/10 levels or the forecasts based on a longer time series. Multiplying the number of shipments by the estimated licence charge provides an initial estimate of the costs to industry of verification. We have also added the estimated administrative costs which are added to these figures. These were initially estimated for 600 shipments in year 1 and have been scaled proportionately for other years / numbers of shipments. This neglects the likelihood that the administrative costs of securing legal timber would be likely to fall overtime, therefore there is likely to be a degree of over estimation of the costs in later years.

**Table 1. Cost per licence, the number of shipments and a delayed Full Cost Recovery regime**

<b>Year</b>	<b>VPA signed - Countries of Export</b>	<b>Estimated number of shipments based upon past volumes and value of shipments including furniture for all VPA countries (Defra)</b>	<b>Updated projected number of shipments from VPA countries based on 2009/10 data (HMRC - figures for Malaysia exclude furniture for now)</b>	<b>Cost per licence (GBP)</b>	<b>Total cost to industry based number of shipments expected associated with past value and volume of shipments (Government charge plus admin cost)</b>	<b>Total cost to industry based on projections associated with 2009/10 shipment data (Government charge plus admin cost)</b>
<b>1 (2012-2013)</b>	Ghana AND/OR Republic of Congo	600	22	£0	£15,800	£579
<b>2 (2013-2014)</b>	Ghana, Republic of Congo, Cameroon, Malaysia	3,000	8,300	£0	£79,000	£218,567
<b>3 (2014-2015)</b>	Republic of Congo, Ghana, Indonesia Malaysia	15,000	29,676	£25	£770,000	£1,523,368

<b>4 (2015-2016)</b>	All above plus Cameroon, Liberia, Central African Republic and Gabon	16,000	29,692	£25	£821,333	£1,524,189
<b>5 (2016-2017)*</b>	All above plus Madagascar and Cote d'Ivoire	17,000	68,468	£25	£872,667	£3,514,691
<b>6 (2017-2018)*</b>	Assumed as above in absense of further information	17,000	68,468	£25	£872,667	£3,514,691
<b>7 (2018 - 2019)*</b>	Assumed as above in absense of further information	17,000	68,468	£25	£872,667	£3,514,691

\* charge to be reviewed after year 4

2.8. The major source of costs to importers is therefore the charge for the Government's check of the licence in advance of the shipment's arrival, and the verification of the shipment's match with the details declared at the border. Other costs which will accrue to importers are those associated with any arrangements that they might need to make in order that they gain possession of the FLEGT licence so that customs formalities can be completed in full by the operator declaring their shipment; we have considered this an administrative costs as follows.

2.9. To estimate the administrative burden imposed by the Regulation, we have undertaken an analysis based upon one manager's work to ensure that shipments will be accompanied by a licence. We envisage that operators would gain assurance that shipments will be accompanied by a licence at the stage when contracts are being negotiated, and would not represent a large or regular ongoing cost (i.e. a cost accrued periodically), because contract negotiation would be undertaken as business as usual. We assume that a particular proportion of operators also undertake a certain amount of negotiation of contracts or ask questions to verify the legality of products purchased, which further reduces the additional cost to businesses above business as usual costs. We have therefore estimated that at least 50% of the work necessary to ensure that a FLEGT licence will be included with each licensable shipment would be undertaken as part of business as usual for the majority of operators.

2.10. Note, these administrative costs to industry, plus the costs of making extra checks for compliance when signing contracts, need to be better understood, however they have been subject to public scrutiny through the consultation process.

2.11. We envisage that the cost imposed by the licence charge will represent a small proportion of the total value of each shipment. This is especially relevant to niche operators which might only import timber and timber products from existing and prospective VPA countries. If the charged levied per shipment for each licence were higher, than such niche operators might be disproportionately affected by the FLEGT licensing scheme. However, because the licence fee

is likely to represent such a low proportion, we are confident that such impacts will be minimal. Average shipment values are estimated to be around £25,000, a £25 fee therefore would represent only 0.1% of the shipment value.

- 2.12. Finally, the number of companies likely to be affected is difficult to judge; we do not have disaggregated data on companies which import timber to the Community market from the FLEGT VPA countries. Rather, we have an aggregated estimate of the total number of shipments likely to be imported annually and apply costs on a per shipment basis.
- 2.13. The costs presented in this summary table represent those costs as they would fall on business; the total costs as faced by government are similar (as this is a Full Cost Recovery scheme), but differently profiled. We may find it appropriate to consult stakeholders closer to the time ahead of the implementation of any new charge.

## **Benefits**

- 2.14. The benefit associated with implementing the FLEGT Regulation is in tackling the serious problems caused by illegal logging globally. The FLEGT Regulation will only apply to those countries which have gone through the process of signing a Voluntary Partnership Agreement with the European Union, and therefore the initial benefits of this Regulation, on a narrow analysis might appear quite modest. However, there is evidence that the VPA signed with Ghana has been an important part of wider governance reform, and has had positive impacts on the country, in terms of the development of new stakeholder engagement processes, and in improving management of the forest sector generally. It is however very difficult to quantify this benefit with a robust or recognised economic methodology. We explain these benefits in detail in the section which follows.

## **The importance of the VPA process for governance reform in the VPA partner country**

- 2.15. Ghana was the first country to sign a VPA with the European Union, and we have therefore decided to explain the benefits to Ghana of the VPA here, because this is the country for which we currently have the most evidenced analysis available. We do however expect that benefits will accrue in similar ways for the other existing VPA, Republic of Congo.
- 2.16. A recent investigation into the benefits and value added by the collaborative VPA process in Ghana, undertaken by the International Institute for Environment and Development, illustrated that the VPA, as per other potential signatory countries, has the potential to alter global market conditions for the timber trade, and in reducing demand for illegal timber, by setting new standards that are likely to influence markets far beyond the EU border<sup>11</sup>. Through removing illegal timber from local markets within VPA countries, the effective implementation of a country's legality assurance system can improve access to key overseas markets, lower the transaction costs nationally of seeking to implement a legal timber market, and increase revenues. The ability of cheap illegal timber and timber products to undercut legal products will be reduced.
- 2.17. Governance reform involves several elements, such as stakeholder engagement in decision making that may not have existed prior to the beginning of the VPA process, for example, increasing transparency and accountability, improved definition and enforcement of land ownership through land tenure reform. This governance reform, and a more transparent business environment in the Ghana, as well as in the other VPA countries, will enable investors

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<sup>11</sup> <http://www.illegal-logging.info/uploads/FLEGTAddingValuereport.pdf>

to measure political risk more effectively, thereby making longer-term investments with confidence, and potentially bringing more capital investment into the country.

2.18. A level playing field in the timber trade sector will also enhance the viability of capital investment in sustainable forestry, attracting investors that are seeking long term yields or socially and environmentally ethical outcomes. A summary of the benefits and losses for Ghana under different scenarios of forest sector reform is presented at Table 2. This has been reproduced courtesy of the Forest Governance Learning Group of the International Institute for Environment and Development.

**Table 2. Gains and losses for Ghana<sup>12</sup> by 2020 under three scenarios - without a legitimate timber regime, with one, and with broader sector reform**

	<b>Gains</b>	<b>Losses</b>
<b>1- Without a legitimate timber regime attempted; i.e. illegal activity continues</b>	<ul style="list-style-type: none"> <li>-Short term profit for some existing industry</li> <li>-Short term benefits for some from chainsaw lumbering</li> <li>-Short-term employment benefits in forest industry</li> </ul>	<ul style="list-style-type: none"> <li>-‘Hard landing’ as sector dwindles fast, corruption rife</li> <li>-Resource crash, deforestation and degraded ecosystem services: foregone carbon payments; soil erosion and water quality problems; and loss of biodiversity</li> <li>-Marginalised communities, rampant illegality, conflict and local governance problems</li> </ul>
<b>2- With an effective legitimate timber regime; i.e. illegal logging tackled</b>	<ul style="list-style-type: none"> <li>-‘Softer landing’ for a downsized sector</li> <li>-Improved formal sector resource management</li> <li>-Increased accountability stimulates positive engagement</li> </ul>	<ul style="list-style-type: none"> <li>-Lower revenues, continued social / environmental risk</li> <li>-Some species loss and forest degradation</li> <li>-Communities still disenfranchised and some social dislocation</li> <li>-Substantial numbers of companies dissolved with employment losses</li> </ul>
<b>3- With sector reform</b>	<ul style="list-style-type: none"> <li>-Stabilised productive forest sector, healthy revenues</li> <li>-Responsible management on and off reserve with maintenance of ecosystem services resulting in carbon storage, watershed and biodiversity protection</li> <li>-Rights, responsibilities and capacity in the best places for good management and local benefit</li> <li>-Larger share of ‘timber economic rent’ to resource owners</li> </ul>	<ul style="list-style-type: none"> <li>-Smaller forest sector</li> <li>-Still lower levels of forest goods and services (may regenerate / expand beyond 2020)</li> <li>-Lower (but sustainable) employment levels</li> <li>-Despite gains – it is too little and too late for some communities</li> </ul>

2.19. Further, it has been quoted that, notwithstanding suggested strengthening and improvements to the VPA process needed in the Republic of Congo, an independent commentator, the Forests and the European Union Resource Network, (FERN), commented that ‘the signed VPA is a remarkable step towards defining a framework to improve forest governance in Republic of Congo’<sup>13</sup>.

2.20. In addition, over time, with the hope that there will be progress on other VPAs moving towards agreement, and with increasing awareness of the availability of FLEGT licensed timber

<sup>12</sup> <http://www.iied.org/pubs/pdfs/G02284.pdf>

<sup>13</sup> [http://www.illegal-logging.info/item\\_single.php?item=presentation&item\\_id=371](http://www.illegal-logging.info/item_single.php?item=presentation&item_id=371)

among buyers and consumers, other prospective VPA partners might also be encouraged to start a VPA negotiation process.

## **Secondary benefits**

- 2.21. A key driver of the trend towards legal timber production, and ultimately sustainable forest management, will be the desire by partner countries to maximise the opportunities presented by forest carbon payments (such as REDD) and similar markets for ecosystem services. Investors in carbon will heavily discount the price of credits backed by forest assets in countries that have opaque governance and a poor record of local democracy and conflict resolution. This means that without the essential governance reforms supported by a process such as that underpinned by a Voluntary Partnership Agreement, nations may not be able to demonstrate readiness to receive REDD payments. Entering a VPA, and installing an effective legality assurance system, may go some way to demonstrate to the carbon markets that the positive changes necessary to receive these payments are afoot, but evidence will need to be 'ground-truthed' to ensure that governance reforms have been implemented.
- 2.22. The IIED Impact Assessment on the VPA process in Ghana does not claim that strategic interests of investors in carbon markets alone will change the outlook for forest management, but there was some evidence to suggest that the needs of investors are beginning to coincide with the needs of timber markets and forest communities, creating a nexus between legal and sustainable timber supplies, good governance, forest carbon programs such as REDD and community economic development. The VPA can be a valuable catalyst in the governance reform process.

## **Benefits in development of the forest products sector, including efforts to eliminate illegal timber products from supply chains globally**

- 2.23. There are also potentially beneficial interactions between the FLEGT licensing scheme required by the FLEGT Regulation 2005, and the proposed Due Diligence Regulation<sup>14</sup> which occur in two ways, and could reduce the cost of meeting the UK's obligations under the latter.
- 2.24. Note that the European Union's proposed timber Due Diligence Regulation has been presented with the objective of complementing and underpinning the EU's current policy framework and support the international fight against illegal logging and its related trade. Firstly, and most simply, the FLEGT Regulation could support a due diligence process for operators by providing a source of timber that is relatively easily identified as legal, i.e. reducing the costs to businesses of 'proving' that timber is legally sourced, thereby providing a 'low risk' source of timber.
- 2.25. Secondly, increasing the supply of legally verified timber could reduce the price premium it receives, therefore decreasing demand illegal sourced, due to its diminished price incentive.
- 2.26. In spite of this it remains a benefit to forest nations to increase the supply of legally verified timber even if there were no premium at all, because timber production is transferred from the illegal to legal sector, with accompanying benefits to government and wider society.
- 2.27. Based on the World Bank analysis which estimated the cost of illegal logging at \$15bn per year. Assuming that the UK takes a share of illegal timber relative to its share of the global timber market, this would imply that by eliminating imports of illegal timber into the UK could generate benefits to timber exporting counties worth approximately £425m per year through

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<sup>14</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0644:FIN:EN:PDF>

increased legal timber trading. To place this cost in context, this is equivalent to 11% of DfID's total expenditure in 2008.

- 2.28. We do not have data which would allow us to disaggregate the proportion of these benefits that would accrue only to those countries which have already signed a VPA, and we therefore do not feel that it is possible at this stage to breakdown benefits in a robust way.
- 2.29. Although initially Voluntary Partnership Agreements with the EU will only cover a small proportion of the wood imported into the UK, to the extent that the production and import of FLEGT licensed timber replaces illegally logged timber it could have significant benefits for those countries involved. If trade in illegal timber is prevented, as opposed to being transferred to other countries which have not signed a Voluntary Partnership Agreement with the European Union, this will result in significant development benefits. This is because a reduction in illegal logging will help the UK to deliver the wider international development and environment objectives of the UK Government.
- 2.30. In summary then, we believe that there is a convincing case that the FLEGT scheme offers net benefits. These emerge in a number of ways, although it is extremely difficult to quantify such benefits reliably.

### **Benefits accruing to importers of FLEGT licensed timber shipments**

- 2.31. As indicated there may be additional administrative costs incurred by timber and timber product traders, and related operators, associated with purchasing the FLEGT verified legal timber. However, there may also be business benefits in terms of the use of certified legal timber, in terms of increased market share, and reputational and Corporate Social Responsibility benefits that they might gain for sale of such timber and timber products. These are not accounted for in this assessment.
- 2.32. Business benefits might also be supported through the changing policy context in Europe, including through further instruments such as the European Commission's proposal for the timber Due Diligence Regulation (described above), and the Government's timber public procurement policy, which states that from April 2009 only legal and sustainable or FLEGT timber will be demanded for use on the Government Estate. This means that FLEGT licensed timber and timber products will be accepted on the Government estate, which will help incentivise further countries to sign VPAs, as well as support the implementation of the Government's sustainable development targets for procurement on its own estate.

### **Assumptions used to produce the analysis**

- 2.33. There are a number of assumptions used to produce the figures in the Impact Assessment: It is only possible to get projected data for timber volumes, as opposed to projected figures on number of shipments, and we have therefore based our analysis on extrapolating data on the number of shipments arriving in the UK in previous years.

We have not captured, or put in any kind of correction / adjustment to take account of the fact that in the past, a particular percentage of undeclared shipments from the countries in question could have cleared UK customs. The shipments included in the data in table 1 are simply the shipments from those countries which Customs have been made aware of.

Changing market conditions over time have not been factored into the future shipment volumes in a significant way.

2.34. The Government will recover both running and set up costs over time, and the payback will therefore accrue as soon as the charge begins, even if that is at a modest level. Full cost recovery will therefore operate over a seven year time period. Waiving any fee for the next two years could therefore be in effect considered a benefit for the 'early' or 'first-movers'. It will also help business to adjust

### **3. Issues of equity and fairness**

3.1. The FLEGT Licensing Scheme introduces questions of equity or fairness to the degree that a level playing field will be created in the marketplace for timber and timber products, because unscrupulous operators who trade in illegal timber will be held to account for their actions.

3.2. Because the FLEGT Regulation puts in place a European Scheme, UK operators will not be disproportionately affected as a result of this scheme.

## Annexes

Annex 1 should be used to set out the Post Implementation Review Plan as detailed below. Further annexes may be added where the Specific Impact Tests yield information relevant to an overall understanding of policy options.

### Annex 1: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. If the policy is subject to a sunset clause, the review should be carried out sufficiently early that any renewal or amendment to legislation can be enacted before the expiry date. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

<p><b>Basis of the review:</b> [The basis of the review could be statutory (forming part of the legislation), i.e. a sunset clause or a duty to review, or there could be a political commitment to review (PIR)];</p> <p>Two years after the entry into force of the first Partnership Agreement the Commission shall present the Council with a report on the implementation of this Regulation, based in particular on the synthesis reports referred to in Article 8(3) and on the reviews of Partnership Agreements. This report shall be accompanied, where appropriate, by proposals for improvement of the FLEGT licensing scheme.</p>
<p><b>Review objective:</b> [Is it intended as a proportionate check that regulation is operating as expected to tackle the problem of concern?; or as a wider exploration of the policy approach taken?; or as a link from policy objective to outcome?]</p> <p>Expected to be a wider review of the policy approach taken, and if these has been effective.</p>
<p><b>Review approach and rationale:</b> [e.g. describe here the review approach (in-depth evaluation, scope review of monitoring data, scan of stakeholder views, etc.) and the rationale that made choosing such an approach]</p> <p>Review of monitoring data from Member States, plus likely detailed questionnaires seeking views from stakeholders.</p>
<p><b>Baseline:</b> [The current (baseline) position against which the change introduced by the legislation can be measured]</p> <p>Currently no FLEGT shipments so baseline is 0 at present (first shipments start arriving around the start of 2012)</p>
<p><b>Success criteria:</b> [Criteria showing achievement of the policy objectives as set out in the final impact assessment; criteria for modifying or replacing the policy if it does not achieve its objectives]</p> <p>Success criteria can be measured by number of FLEGT licences processed, and number of goods detected at the border without valid FLEGT licences, and number of prosecutions.</p>
<p><b>Monitoring information arrangements:</b> [Provide further details of the planned/existing arrangements in place that will allow a systematic collection of monitoring information for future policy review]</p> <p>Member States shall be required to submit by 30 April an annual report covering the previous calendar year, which shall include the following:</p> <ul style="list-style-type: none"><li>(a) quantities of timber products imported into the Member State under the FLEGT licensing scheme, as per HS Heading specified in Annexes II and III and per each partner country;</li><li>(b) the number of FLEGT licences received, as per HS Heading specified in Annexes II and III and per each partner country;</li><li>(c) the number of cases and quantities of timber products</li></ul>
<p><b>Reasons for not planning a review:</b> [If there is no plan to do a PIR please provide reasons here]</p>



## Annex 2: Outcome of Impact Tests not referred to in the Evidence Base

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

Type of testing undertaken	Results in Evidence Base?	Results annexed?
Competition Assessment	No	Yes
Small Firms Impact Test	No	Yes
Legal Aid	No	Yes
Sustainable Development	No	Yes
Carbon Assessment	No	Yes
Other Environment	No	Yes
Health Impact Assessment	No	Yes
Race Equality	No	Yes
Disability Equality	No	Yes
Gender Equality	No	Yes
Human Rights	No	Yes
Rural Proofing	No	Yes

### Competition assessment

All timber and timber product importers in the UK will be subject to the requirements of the FLEGT licensing scheme. It is not felt that these requirements will reduce the number or range of importers of the relevant products nor limit the ability of consumers to choose the price, range, quality and location of their products. The measures will not impose additional costs on new entrants compared to incumbent firms, other than the need for all operators to ensure that timber and timber products will be exported legally, and potentially to write this in to their contracts with supplying exporters in VPA countries. The industry is not characterised by rapid technological change per se, but UK timber importers are world leaders in chain of custody monitoring and legality verification, and the legality verification of a FLEGT licence will support this competitive advantage internationally (outside of the EU) for any value-added manufactured exported products from the UK. All EU Member States will need to implement the legislation so there will be a more level playing field for EU competition, and the gradual elimination of unscrupulous operators who import illegal timber will also level the market playing field.

### Small Firms Impact Test

There are no exemptions for small firms from implementing the FLEGT Regulation. The Government is not currently planning to charge for its work to check, administer and verify FLEGT licences, in the first two years of operation of the FLEGT scheme. This will help to

reduce the burden on small business, as per all businesses, by providing them with two years to ensure that they put in practice measures to ensure a FLEGT licence is provided. On the introduction of a possible charge for the FLEGT licence check from year three onwards, there may be uneven impacts on niche importers, which only import from VPA countries, but given that the likely scale of a charge on operators is almost certain to be a small proportion of the total value of any shipment, we are confident that no operator will be disadvantaged by the FLEGT licensing scheme.

### **Legal Aid**

New domestic legislation putting into effect the FLEGT licensing scheme [in the UK] may create a new penalty for producers who fail to comply with the requirement to produce a FLEGT licence for licensable shipments. We are consulting stakeholders on whether such a new offence is necessary. The penalties for such an offence could take a number of forms, such as a monetary offence. A producer who refused to pay a penalty would risk prosecution. A producer who faced prosecution in this circumstance would not be eligible for legal aid.

### **Sustainable Development**

The FLEGT Regulation is in accordance with UK principles of sustainable development.

### **Carbon Impact Assessment**

The FLEGT Regulation supports the European Union's efforts to tackle global deforestation, given that it supports a process of governance reform in the VPA countries. To this extent, and because of avoided illegal logging, the FLEGT Licensing scheme contributes to reducing carbon emissions. It is not possible to quantify the exact reduction due to the complexity of the sector.

### **Other Environmental Issues**

As the FLEGT licensing scheme will still involve harvesting timber, some environmental impacts are likely to remain the same. However, because it is part of a wider programme of reform which could lead to sustainable forest management, the FLEGT licensing scheme could have beneficial secondary implications in relation to climate change, landscape preservation, water and floods, habitat and wildlife. Waste management and noise pollution are unlikely to be affected.

### **Health Impact Assessment**

The FLEGT licensing scheme could potentially have a secondary positive impact on health by an increased level of concern for health and safety practices in logging operations. We do not currently have any data to support this.

### **Race /Disability/Gender**

The FLEGT licensing scheme does not introduce any questions of equity or fairness in terms of race, disability or gender, other than that the governance reform in VPA countries could have a number of positive impacts for all citizens of those countries, as well as levelling the playing field for European operators generally, through reducing the number of unscrupulous operators who undercut their businesses.

### **Human Rights**

The FLEGT licensing scheme is consistent with the Human Rights Act 1998.

### **Rural Proofing**

The FLEGT licensing scheme will not have any impact on the rural community in the UK, although rural businesses in VPA countries will benefit from the wider reform process of which the FLEGT licensing scheme plays a part.