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Verified Legal? Ramifications of the EU Timber Regulation and Indonesia's Voluntary Partnership Agreement for the Legality of Indonesian Timber

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SUMMARY

The EU Timber Regulation bans illegal timber in Europe and requires due diligence on imported wood. Given the recent ratification of the EU-Indonesia Voluntary Partnership Agreement (VPA), the Timber Regulation raises questions about the role that Indonesia's timber legality certification scheme—the SVLK—plays in securing access for Indonesian timber to the European market. Certified timber automatically qualifies for export to Europe under the VPA, but the SVLK has weaknesses which the VPA may be unable to address. The Timber Regulation might have helped, but it explicitly excludes VPA timber from its due diligence requirements. Critically, though, it continues to apply to Indonesian timber entering the EU via third countries. Whether it can address the SVLK's shortcomings as regards this timber depends on: (1) whether the SVLK meets the Regulation's certification scheme reliability criteria; and (2) whether the EUTR considers certification sufficient proof of legality to satisfy due diligence requirements.

Keywords: illegal timber, SVLK, EUTR, VPA, FLEGT

Ramifications légales? vérifiées de la Régulation européenne du bois et de l'Accord de partenariat volontaire indonésien pour la légalité du bois indonésien

A. FISHMAN et K. OBIDZINSKI

La Régulation européenne du bois bannit le bois illégal en Europe et insiste sur un contrôle diligent du bois d'importation. Du fait de la ratification récente de l'Accord de partenariat volontaire entre l'Europe et l'Indonésie (VPA), la Régulation du bois remet en question le rôle que le système de certification de légalité du bois indonésien- le SVLK- joue pour assurer l'accès du bois indonésien au marché européen. Le bois certifié est automatiquement qualifié par le VPA à l'exportation vers l'Europe, mais le SVLK a des faiblesses que le VPA n'est pas forcément à même de résoudre. La régulation du bois aurait peut-être pu être utile, mais elle exclut explicitement le bois du VPA de ses critères de surveillance. Elle continue cependant à les appliquer au bois indonésien atteignant l'Union Européenne par des pays tiers. Elle pourrait prendre en charge les faiblesses du SVLK si, (1) le SVLK atteint les critères de fiabilité du processus de certification de la Régulation et, (2) si l'EUTR considère que la certification est preuve suffisante de légalité pour satisfaire aux critères en place.

¿Legalidad verificada? Ramificaciones del Reglamento de la Madera de la UE y el Acuerdo Voluntario de Asociación de Indonesia para la legalidad de la madera de Indonesia

A. FISHMAN y K. OBIDZINSKI

El Reglamento de la Madera de la UE prohíbe la madera ilegal en Europa y requiere la diligencia debida en la madera importada. Dada la reciente ratificación del Acuerdo Voluntario de Asociación (AVA) entre la UE e Indonesia, el Reglamento de la Madera plantea interrogantes sobre el papel que desempeña el sistema de certificación de la legalidad de la madera de Indonesia (SVLK, por sus siglas en indonesio) en cuanto a garantizar el acceso de la madera de Indonesia al mercado europeo. La madera certificada califica automáticamente para la exportación a Europa bajo el AVA, pero el SVLK tiene debilidades que es posible que el AVA no pueda solventar. El Reglamento de la Madera podría haber ayudado, pero excluye explícitamente la madera AVA, debido a sus requisitos de diligencia debida. Sin embargo, es primordial que sigue siendo relevante para la madera de Indonesia que entra en la UE a través de terceros países. El que pueda abordar las deficiencias del SVLK en cuanto a esta madera depende de: (1) si el SVLK satisface los criterios de fiabilidad del sistema de certificación del Reglamento; y (2) si el EUTR considera la certificación como prueba suficiente de legalidad con la que satisfacer los requisitos de diligencia debida.

INTRODUCTION

Over the past decade, the EU has become a leading supporter of timber legality verification—a technique whereby traded timber is restricted unless it complies with the relevant laws of the country in which it was harvested. In principle, legality verification, if broadly adopted and enforced, should eliminate foreign demand for illegal timber and reduce the contribution of illegal logging to deforestation.

The EU promulgated the Forest Law Enforcement, Governance and Trade (FLEGT) Regulation in 2005, which created a market incentive to curb illegal logging. The Regulation established a framework for trade partners to negotiate Voluntary Partnership Agreements (VPAs) with the EU under which their timber products can only be exported to the EU with a license evincing legality (FLEGT Regulation 2005).

Indonesia began negotiating a VPA in 2007, and the agreement entered into force in March, 2014 (EIA 2014). Under the VPA, Indonesia uses its *Sistem Verifikasi Legalitas Kayu* (SVLK) to verify the legality of its timber, and the resulting certification forms the basis for awarding FLEGT licenses (VPA 2014: arts. 2, 3, 6, & 7). Observers have voiced misgivings, however, regarding the SVLK's robustness. Some worry, for example, that it provides for insufficient monitoring, and that under-capacity and conflicts of interest will render verification impotent (Luttrell *et al.* 2011).

The entry into effect in March 2013 of the EU's second piece of anti-illegal logging legislation—the EU Timber Regulation (EUTR)—raises the question of whether this Regulation might address the gaps in the SVLK. The EUTR complements the VPA mechanism by banning the import of illegal timber from all countries and obligating importers to implement due diligence systems to minimize their risk of handling illegal products. If these requirements can be understood to underpin a negotiated VPA, they may 'fix' the problems with the SVLK and ensure that no illegal timber is able to enter the EU.

This paper examines the relationship between the SVLK and the EUTR. The following two sections analyze each, respectively, in order to provide a basis from which to assess the status of Indonesian timber vis-à-vis the EU. The subsequent section performs this assessment, examining the relationship between these two instruments and explaining the relevance of the EUTR to Indonesian timber. The authors draw on prior research concerning timber trade flows and the robustness of the SVLK, and introduce original legal analysis of the EUTR to inform this assessment.

INDONESIA'S TIMBER LEGALITY ASSURANCE SYSTEM (THE SVLK)

Initially authorized by the SVLK Regulation in 2009 and subsequently modified several times, the SVLK seeks to ensure that all timber in Indonesia's supply chain is harvested, transported, and processed in accordance with Indonesian law. Timber harvesters and processors are required to obtain certification, at their own expense, demonstrating that their

timber operations are conducted legally (SVLK Regulation: art. 7.4). Failure by an exporter to present a valid legality certificate can lead to consequences including denial of an export license and prosecution (Trade Ministry Regulation: art. 21).

Legality certificates are awarded by Independent Assessment and Verification Agencies (LP&VIs), which inspect timber operations for conformity with one or more of four "legality definitions" (SVLK Regulation: art. 2). Timber harvested in state-owned forests, for example, is legal when the harvester is authorized to operate in the area, and when procedural and substantive harvest laws have been adhered to (Ibid: Annex 2). Timber originating in privately owned forests need only be accompanied by proof of ownership (Ibid: Annex 5). Timber harvested in land designated for clearing requires proof that clearing activity is authorized and compliance with relevant timber harvest and transport laws (Ibid: Annex 6). Certification of processed timber requires proof that processors are authorized to operate and that a timber tracing system is in place (Ibid: Annex 4). As Indonesia prohibits the export of unprocessed wood (Prasetyo *et al.* 2012), all timber exports must meet the legality standard both for processed timber and for the area type from which the raw timber was harvested.

If the auditee objects to the result on an inspection, he or she may submit the objection to the auditing LP&VI, and the LP&VI will establish an independent ad-hoc team to evaluate the objection and correct the audit if appropriate (SVLK Regulation: arts. 9.2–9.4). If the timber operation fails the audit, it must be given an opportunity to come into compliance with the applicable legality definition (Ibid: art. 12.3). The result upon successfully passing an audit depends on the type and size of the auditee. Harvesting operations in state-owned forests, forests designated for conversion, and large timber processors become certified for three years, but remain subject to annual surveillance audits (Ibid: art. 10.4). Small timber processors become certified for six years and must be audited at least every two years (SVLK Amendment 2012: art. 1.4). Private forest owners that send timber for processing become certified for ten years and must also be audited every two (Ibid: art. 1.5–1.6).

Individuals, NGOs, and civil society groups may challenge an LP&VI's audit of a timber operation (SVLK Regulation: arts. 14.2–14.3; SVLK Amendment 2011: art. 1.1). If the LP&VI "cannot resolve the issue of objection," the challenging party may bring its complaint to the national body that accredits LP&VIs (SVLK Regulation: art. 14.3). The meaning of this quoted phrase is ambiguous and raises the question of whether the accreditation body functions as a forum for appeal. If the phrase refers to a situation where the LP&VI does not resolve the matter to the challenging party's satisfaction, then recourse to the accreditation body effectively constitutes an appeal of the LP&VI's decision. If the phrase instead refers to a situation where the LP&VI is unable to arrive at a decision concerning the challenge, then recourse to the accreditation body is unavailable so long as the LP&VI makes a decision, and there is no scope for appeal. Regardless

of the interpretation, the SVLK does not authorize appeal to the courts.

A multi-stakeholder monitoring and evaluation working group provides additional monitoring by reviewing independent monitoring reports and other information sources to track SVLK implementation (EFI n.d.). In the context of the VPA, several additional mechanisms monitor the timber sector and the SVLK. First, the Agreement creates a system of annual “periodic” evaluation to review the functioning and effectiveness of the SVLK’s legality control measures and timber traceability systems (Draft VPA: art. 15(a)). Second, it requires the EU to appoint every two years an “Independent Market Monitor,” which will assess how Indonesian timber bearing FLEGT licenses is performing in the European market (Ibid: art. 15(b) & Annex VII). On the basis of the reports from these two mechanisms, a Joint Implementation Committee comprising Indonesian and EU appointees will review the overall functioning of the SVLK (Ibid: art. 14.5(b)). Finally, the VPA mandates a one-time independent technical evaluation of the SVLK before issuance of FLEGT licenses commences (Ibid: art. 14.5(e)), to check whether the SVLK delivers the intended results in practice and to examine any revisions Indonesia has made to the SVLK since signing the VPA (Ibid: Annex VIII). The VPA additionally requires both Indonesia and the EU to monitor the impacts of the VPA on indigenous and local communities, but does not establish an instrument to implement this obligation (Ibid: art. 12.2).

THE EU TIMBER REGULATION (EUTR)

Understanding the relevance of SVLK certification to Indonesian timber that enters the EU requires some analysis of the EU regulation that governs timber imports. This section analyzes the EUTR and the following section considers how the SVLK interacts with it.

The EUTR’s central provision is a ban on introducing to the European market timber or products made from timber harvested in violation of the laws of the country of harvest (EUTR: art. 4.1). Supplementing this ban, the Regulation imposes obligations on entities that place timber or products thereof on the European market for the first time (“operators”), and on entities that buy or sell such timber or timber products (“traders”). The requirements that pertain specifically to traders are fairly straightforward, functioning merely to ensure that the timber and timber products that traders deal in can be traced along the supply chain (Ibid: art. 5).

Operators face somewhat more demanding requirements. To ensure that they do not place illegally harvested timber or timber products on the European market, operators must exercise “due diligence” (Ibid: art. 4.2). This involves three steps: information-gathering, risk assessment, and risk mitigation. The first step is designed to ensure that operators possess adequate information concerning the timber or timber products in their inventory to perform useful risk assessment (Ibid: art. 6.1(a)). Once risk assessment is completed, operators are required to mitigate any identified risk that is more than “negligible” (Ibid: art. 6.1(c)).

The middle stage of the due diligence process—risk assessment—is meant to provide helpful analysis to inform subsequent risk mitigation activities. Operators must evaluate the likelihood that the timber which they introduce to the market was harvested illegally. The Regulation provides a list of specific risk assessment criteria to consider, but the list is non-exhaustive; additional criteria may be considered if they help determine the timber’s legal status. Criteria that must be considered include information specific to the timber or timber product at issue, and information about the context in which harvesting took place. Critically for our purposes, operators must consider assurance of compliance with applicable legislation (Ibid: art. 6.1(b)), defined essentially as any legislation in force in the country of harvest which concerns rights and obligations associated with timber harvesting (Ibid: art. 2(h)). Assurance of compliance with these laws may be provided by certification or another third-party verification scheme (Ibid: art. 6.1(b)).

Operators and traders that violate their obligations under the EUTR are subject to penalties, but EU Member States are granted wide discretion to choose their form and severity (Ibid: art. 19). Equally as importantly, Member States must each decide whether violations require a particular level of intent to warrant penalty. Penalty design may strongly affect the level of risk that operators are likely to embrace in choosing to deal in timber with a specter of illegality. Severe penalties combined with the possibility that operators could be found liable for mere negligent violations, or even for violations lacking any culpability (i.e., a ‘strict liability’ standard) could significantly chill imports from sources with even a hint of illegality. Such penalties would strongly incentivize timber-exporting countries to negotiate VPAs, to eliminate the uncertainty that operators face in deciding whether to deal in their timber.

CAN THE EUTR ADDRESS WEAKNESSES IN THE SVLK?

The SVLK has been hailed as an important tool for promoting legality in the Indonesian forestry sector (EIA 2013), but there are a number of concerns regarding the SVLK’s robustness, both in its design and the way it has been implemented. Given these gaps, the relationship between the SVLK and the EUTR becomes particularly relevant. To what extent will the Regulation’s illegal logging provisions apply to SVLK-certified timber after the VPA is ratified? Can the EUTR serve as a backstop to support the Indonesian VPA’s measures to promote legal logging? If so, can evidence of legality additional to SVLK certification be required of operators? The first subsection that follows discusses the gaps in the SVLK which would make application of the EUTR desirable. The second subsection analyzes whether the EUTR can in fact fill in these gaps and the role that the SVLK plays in applying the EUTR to Indonesian timber. The final subsection considers the extent to which the EUTR authorizes demands for proof of legality above and beyond SVLK certification.

Gaps in the SVLK

A basic concern with the SVLK is that its task is simply too massive to be carried out effectively. There are too many timber harvesting and processing units to evaluate, and too complex a legal framework against which to evaluate them. It is not even clear how many units there are; one source estimates 10,000 (Adams & Asycarya 2012), while another credits Java alone with 121,438 handicraft and small furniture businesses that use timber (Sudharto 2012). Either way, only 632 were certified by December 2013 (ITTO 2014), and the full compliance of even these units may be suspect given that around 800 Indonesian laws pertain to forests, and, in the words of one commentator, “ensuring conformity with all national and local laws may be factually impossible” (Brown 2008: 257). It has been argued that the SVLK does not in fact require compliance with all regulations that are relevant to forestry (Anti Forest-Mafia Coalition 2014).

Scale of the task and complexity aside, capacity constraints limit the pace and effectiveness of the auditing process. When the SVLK became mandatory, only four evaluators were capable of performing legality verification. Although this number has risen, it has done so slowly, to eleven by May, 2013 (Lubis 2013a), and fifteen at present (ITTO 2014b). Evaluators are scarce because few people in Indonesia are properly trained to carry out SVLK audits (as of 2011 there were only 150) (Luttrell *et al.* 2011). Besides limiting the feasibility of auditing all the players involved in Indonesia's sizeable annual timber output, this scarcity may create unavoidable conflicts of interest. LP&VIs and the auditors they employ are required to meet accreditation and other requirements (Director General Regulation 2010: Annex 6, art. II-III), but these may be unrealistic when the pool of trained auditors is so small and when so many of them, understandably, have close industry ties (Luttrell *et al.* 2011).

A certain risk of conflict of interest is built into the SVLK. The first round of timber legality verification is financed by the Ministry of Forestry (SVLK Regulation: art. 7.2), but future verification costs are to be borne by auditees (Ibid: art. 7.4). This will likely tempt auditors to be lenient in their assessments of timber operators so as not to bite the hand that feeds them (Luttrell *et al.* 2011), much the same way that credit rating agencies understated the risk inherent in the debt sold by the investment banks that hired them, helping launch the subprime mortgage crisis (Buttonwood 2007). Meanwhile, auditors might simultaneously experience a conflict of interest going up the oversight hierarchy if the Indonesian government provides them with the “technical skill or financial assistance” which the SVLK Regulation authorizes it to (SVLK Regulation: art. 15.1).

Any conflicts of interest would be especially problematic because the scoring system that auditors use to verify legality under the SVLK is highly permissive. Certification may be granted even to companies that only achieve a score of ‘FAIR,’ and it is “very easy for auditors to avoid scoring a company's performance as ‘POOR’” (Anti Forest-Mafia Coalition 2014: 8). There is also no requirement that auditors conduct

chain of custody verification, allowing timber mills to become certified even if they process timber from lands that are not SVLK certified (Ibid).

Other design features of the SVLK may also give cause for concern. First, the definition of “legal” timber, when harvested from state-owned forests, defers the environmental and social obligations that it encompasses to environmental impact assessments and associated documents. These documents describe the measures that forest operators must take to mitigate their environmental impacts and to protect the interests of people who depend on the forest in which they operate (EFI n.d.). The SVLK simply requires LP&VIs to verify that these environmental and social protections exist and are being implemented, leaving a great deal of discretion to the government body that approves these documents.

The situation concerning timber harvested from private forests and forests designated for conversion is perhaps even more alarming. Whereas the legality definitions for the other forest types include such requirements as possession of valid equipment licenses and proper marking of logs for purposes of supply chain tracking, timber harvested from private and conversion forests can be deemed legal without meeting these requirements.

An additional design flaw is that the SVLK imbues LP&VIs with a great deal of responsibility, authorizing them to evaluate timber operations, issue legality certificates, and respond to objections raised concerning their own activities. Such a concentration of responsibility within one institution may expose the system to capture by interest groups (Luttrell *et al.* 2011). Moreover, the multiplicity of licensing authorities which the SVLK permits (unlike the timber legality assurance systems required by VPAs negotiated with other countries) adds complexity. Although this approach has been justified as necessary due to Indonesia's large size and decentralized government, and although national accreditation should provide a level of consistency among licensors, there remains a fear that the result could be uneven application of the SVLK (Ibid).

Commendably, the SVLK features an independent monitoring mechanism that may help in preventing these outcomes, but this may not be sufficient to allay fears that legality verification will be executed improperly. Fundamentally, the role that the SVLK authorizes independent monitors to play is fairly circumscribed. Unlike the higher level monitoring mechanisms that the VPA requires, independent monitors are limited to bringing complaints concerning individual assessments of timber operations, meaning that they cannot lodge more general complaints. (Although the multi-stakeholder monitoring group which the Ministry of Forestry Director General's decree created is tasked with conducting more systemic monitoring, the results of its monitoring efforts are confined to recommendations, which legally need not be entertained.) Independent monitors also have no opportunity to appeal decisions concerning their complaints to the courts, and may not be able to appeal to the accreditation body either, depending, as discussed earlier, on the interpretation of the phrase “cannot resolve the issue of objection.”

As a practical matter, Indonesian civil society may not have the capacity to carry out effective monitoring (Ibid). Moreover, hurdles impede its ability to access relevant information. Despite requirements that information be made public, some key documents such as planning documents and maps are not always published (Anti Forest-Mafia Coalition 2014). JPIK—Indonesia’s Independent Forestry Monitoring Network—has noted the significant difficulty that civil society has in accessing relevant information for monitoring (JPIK 2013), and the head of the Environmental Investigation Agency’s Forests Campaign Team has gone a step further, observing that “[t]here is absolutely no system of information for the SVLK [sic] implementation that is up and running and accessible” (EIA 2013).

A second practical challenge is that implementation of the SVLK could have the unintended effect of shutting small actors out of the market. Legality certification costs Indonesian companies between Rp 60 million (US\$6,120) and Rp 100 million (US\$10,200) (Lubis 2013)—which may be beyond what many small actors can afford (Obidzinski *et al.* 2014)—and requires a complex administrative process that exceeds the management capacity of most small timber enterprises (ITTO 2013b). Only fifteen of Indonesia’s tens of thousands of small-scale timber processors have been awarded SVLK certificates to date (Obidzinski *et al.* 2014).

Whatever the anticipated challenges with the SVLK, the experience of the first few years of implementation has revealed certain weaknesses. There continues to be “widespread violation of Indonesian laws by certified companies” despite these companies having been certified as SVLK-compliant (Anti Forest-Mafia Coalition 2014: 10). Reports have surfaced that LP&VIs are not fully auditing timber processors that possess timber utilization permits and that claim to source their timber from conversion forests, on the assumption that these permits attest to legal operation. Other reports criticize the mechanism for addressing civil society complaints as weak, with many complaints receiving inadequate responses or being ignored entirely (EIA 2013). There have even been reports of human rights violations on lands managed by SVLK certified companies (Human Rights Watch 2013).

Relationship between the SVLK and the EUTR

In light of these concerns, one question is whether there is any scope for the EU to restrict imports of SVLK-certified timber (i.e., all Indonesian timber, since the SVLK Regulation requires that all timber be certified). One thing that is certain is that ratification of the VPA means that certified Indonesian timber exports to the EU will be virtually unimpeachable once they commence. The EUTR is explicit that timber traded under a ratified VPA need not satisfy the EUTR’s other provisions: VPA timber must be accompanied by a FLEGT license, and possession of a license is sufficient proof of legality for purposes of the Regulation (EUTR: art. 3), obviating the need for operators to perform due diligence. The Indonesian VPA recognizes the SVLK as the system for verifying the legality of Indonesian timber exports (VPA: preamble), so ratification

has concretized SVLK certification as the basis for exempting operators from having to carry out due diligence on timber shipped from Indonesia (FERN 2013, ITTO 2013). FLEGT-licenses will begin to be awarded to Indonesian timber once the EU and Indonesia agree that the SVLK meets the VPA’s requirements (Minangsari 2014).

The VPA provides for “periodic evaluation” and a two-yearly independent monitoring mechanism, the findings of which the Joint Implementation Committee may cite in deciding on “remedial measures” to the VPA (VPA: art. 14.5(b-c)). This mechanism provides the EU an opportunity to adjust the requirements for obtaining a FLEGT license, and may give it leverage in requesting changes to a faulty SVLK scheme. However, the Joint Implementation Committee, tasked with “consider[ing] issues related to the implementation and review of [the VPA],” is staffed by European and Indonesian officers, and its decisions are taken by consensus (Ibid: art. 14.1–14.2). Indonesian officers may not easily accede to adjustments requiring revisions to national legislation which has already been in place for six years, has undergone multiple rounds of reform, and which the forest sector already considers to be overly burdensome—especially after the EU repeatedly delayed ratification of the VPA (Lubis 2013b). The EU will be free to seek recourse at a higher level and request an amendment to the VPA itself, but change could only become binding with Indonesia’s consent (VPA: art. 22.1). The EU could also temporarily suspend, permanently terminate, or renounce extension of the VPA (Draft VPA: arts. 21, 23.3–23.4), but any of these actions would simply cause regulation of Indonesian timber exports to default to the EUTR, which is what the EU looked to avoid by negotiating a VPA in the first place.

Although the VPA has replaced the EUTR in governing the Indonesia-EU timber trade, it does not render the EUTR entirely impotent with respect to Indonesian timber. The VPA only governs timber that is exported from Indonesia to the EU, and is unconcerned with timber that enters the European market from other points of departure. Thus, the EUTR applies where Indonesia exports timber products (which are covered by the Regulation) to a third country, which then re-exports or reprocesses and then re-exports them to the EU.

The EUTR suffers from several weaknesses and is thus not a fail-safe against imports of illegal timber. For example, its prohibition on placing illegal timber on the EU market applies only to actors that place timber on the market *for the first time*, creating a loophole whereby shell companies could be created to place illegal timber on the EU market while protecting repeat players. Even without such manipulations, illegal timber can be freely shipped to the EU in the form of printed paper or other products that fall beyond the Regulation’s scope. Additionally, the flexibility which the EUTR leaves to Member States to design penalty provisions could result in penalties that do little to deter illegal trade (Levashova 2011). Indeed, the World Wildlife Fund has determined that 15 of 28 Member States have not done enough to address trade in illegal wood (WWF n.d.). Finally, the fact that the EUTR exempts from its core requirements timber that bears a certificate under the Convention on International

Trade in Endangered Species of Wild Fauna and Flora (CITES) increases the likelihood that illegal timber could enter the EU because the definitions of legality under CITES and under the EUTR differ from one another (Saunders & Reeve 2014).

Despite these weaknesses, the EUTR sends a clear message to the international market that illegal timber is unacceptable in the EU. Further, it provides regulators with a legal basis for beginning to crack down on illegal timber shipments. While the EUTR does not apply to timber shipped from Indonesia directly to the EU, its provisions do apply to imports of Indonesian timber that arrive via third countries, and can thus serve to backstop the SVLK in the event that illegal timber is able to circumvent Indonesia's legality verification system.

It is difficult to know how much of Indonesia's timber exports to third countries ultimately continues on to the EU because countries tend not to report what ultimately becomes of imported timber. Somewhat mitigating the likelihood that the quantity of indirectly imported Indonesian timber is large is the fact that Indonesia prohibits the export of unprocessed wood (Prasetyo *et al.* 2012). Consequently, timber products shipped from Indonesia to third countries and then on to Europe are legally limited to semi-processed products that undergo further processing in the third countries, or finished products that are merely transshipped.

At the same time, Indonesia exports a great deal of its forestry products to third countries that are important sources of imports to the EU. In 2011, over half of Indonesian forest product exports went to the EU's top ten trade partners (see Tables 1 and 2). It may thus be reasonable to assume that a non-insignificant quantity of Indonesian timber finds its way to Europe from other countries.

However much the amount, those Indonesian timber products (covered by the EUTR) that reach the EU via a third country fall under the EUTR's due diligence provision. The

TABLE 1 *EU Imports from its Top Ten Trade Partners in 2011*

Country	Imports (million €)	Share of EU imports
China	289,902	16.2%
Russia	212,882	11.9%
USA	205,170	11.5%
Switzerland	104,564	5.8%
Norway	100,152	5.6%
Japan	63,868	3.6%
Turkey	47,845	2.7%
South Korea	37,855	2.1%
India	37,328	2.1%
Brazil	37,254	2.1%

European Commission, n.d.

TABLE 2 *Indonesia's Forest Product Exports in 2011 to the EU's Top Ten Trade Partners*

Country	Exports (thousand US\$)	Share of Indonesian Exports
China	1,531,000	19.97%
Russia	10,000	0.13%
USA	312,000	4.07%
Switzerland	505	0.01%
Norway	5,969	0.08%
Japan	1,467,000	19.14%
Turkey	56,000	0.73%
South Korea	458,000	5.97%
India	251,000	3.27%
Brazil	21,891	0.29%

FAO, n.d.

impact of SVLK certification on the due diligence requirements becomes relevant for this segment of Indonesia's timber, and any concerns regarding the robustness of the SVLK assume significance. The question, then, is to what degree does SVLK certification satisfy operators' due diligence obligations?

The answer lies with the due diligence provision's risk assessment criteria, which determine the degree of risk that operators assume when they deal in particular timber. The key criterion is "assurance of compliance with applicable legislation, which may include certification or other third-party-verified schemes which cover compliance with applicable legislation" (EUTR: art. 6.1(b)). Given this language, there are two reasons why SVLK certification may not suffice in and of itself. First, the SVLK, as designed, may not constitute a valid "assurance of compliance." Second, even if it does, assurance of compliance is only one factor to consider and is probably not itself sufficient to satisfy due diligence.

Although the EUTR lists legality certification as a risk assessment criterion, it defers further elaboration of the due diligence requirements to a future regulation (Ibid: arts. 6.2–6.3). A clarifying regulation adopted in 2012 limits consideration of certification schemes to those that: (1) have a publicly available system of requirements which includes the relevant requirements of all applicable national laws; (2) require at least annual audits by third parties which include field visits; (3) include timber supply chain tracking mechanisms; and (4) include means of ensuring that illegally harvested timber is excluded from the market (Due Diligence Implementing Regulation: art. 4).

It is likely that the SVLK does not meet these criteria. As to the first requirement, the primary regulations which establish and flesh out the SVLK are indeed publicly available on the Ministry of Forestry website.¹ And, while a full inquiry into whether the SVLK's legality definitions oblige verifying

¹ The website is <http://www.dephut.go.id/index.php?q=id/node/5459>.

bodies to check for compliance with all relevant laws exceeds the scope of this paper, it may be reasonable to interpret the SVLK itself—duly enacted by the Indonesian government—as containing the requirements that Indonesia deems relevant.

The second requirement—that the verification scheme require at least annual audits by third parties which include field visits—is only partly met. The SVLK requires LP&VIs to conduct yearly audits of certified harvesting operations in state-owned forests and forests designated for conversion, as well as of certified large timber processors. Meanwhile, small timber processors and private forest owners need only be audited every two years. In addition, field verification is required only for certain of the legality criteria pertinent to timber harvested in state-owned forests.²

The requirement of a mechanism for tracking timber along the supply chain is met, although only by virtue of legal obligations external to the SVLK. The legality definitions for timber harvested from state-owned forests and for processed timber require that logs be barcoded or otherwise marked to ensure traceability. There is no explicit requirement that timber harvested from private forests or from forests designated for conversion be marked, but the standing ban on the export of unprocessed timber forces all timber that might reach Europe to undergo processing, and therefore application of supply chain tracking measures. Lifting of this ban in the future could thus undermine supply chain tracking if traceability requirements are not simultaneously extended to logs taken from private forests and forests designated for conversion.

It is unclear whether the fourth requirement—that the verification scheme include a means of ensuring that illegally harvested timber is excluded from the market—is satisfied. Timber may not be exported unless it is SVLK certified, but because certification is valid for 3–10 ten years and because timber operations need only be audited once every year or two, it is possible that individual export shipments falling between audits could contain illegal timber despite the existence of valid certification. Reliance on export restrictions pegged to periodic legality audits may suffice, however, because the EUTR is not specific about the way in which illegally harvested timber must be excludable from the European market.

If SVLK certification were held to constitute valid “assurance of compliance,” the EUTR probably does not conceive of third-party verification schemes as being sufficient to satisfy due diligence obligations. The primary evidence is that the “assurance of compliance” risk assessment criterion is only one of several that the Regulation requires operators to account for in exercising due diligence. So long as other risk assessment criteria may be considered “relevant,” they must be taken into account.

Further evidence is the fact that the clarifying regulation concerning due diligence amended the due diligence requirements to provide that “[c]ertification or other third-party

verified schemes ... may be taken into account” (Due Diligence Implementing Regulation: art. 4). Replacing the word “shall” with “may” transforms assurance of compliance mechanisms from mandatory criteria, as they seemed to be in the original EUTR, into permissive criteria. Given that assurance of compliance is only one of several risk assessment criteria and that its consideration is not even obligatory, an operator probably could not point to SVLK certification to satisfy its due diligence obligations, even if the SVLK were deemed to meet the EUTR’s definition of a reliable certification scheme.

Extent of the EUTR’s Requirement of Proof of Legality

Although SVLK certification cannot form the sole basis for satisfying the “assurance of compliance” element of the EUTR’s risk assessment criteria, the scope of the due diligence requirements is not boundless. The due diligence provision only speaks of “assurance of compliance *with applicable legislation*” (EUTR: art. 6.1(b), emphasis added), defined as:

[L]egislation in force in the country of harvest covering the following matters:

- rights to harvest timber within legally gazetted boundaries,
- payments for harvest rights and timber including duties related to timber harvesting,
- timber harvesting, including environmental and forest legislation including forest management and biodiversity conservation, where directly related to timber harvesting,
- third parties’ legal rights concerning use and tenure that are affected by timber harvesting, and
- trade and customs, in so far as the forest sector is concerned (EUTR: art. 2(h)).

This list is exhaustive, so operators cannot be required to demonstrate compliance with any laws that do not fit into one of these categories. Notably absent from the list is any reference to legislation designed to ensure transparency in the forestry sector or provision of notice to or consultation with impacted communities. In other words, while the EUTR is concerned with the impacts of illegal logging on “legal rights concerning use and tenure,” it is not concerned with other social impacts. Communities with customary rights not recognized by the formal legal system, for instance, are not protected.

Nonetheless, it may be that laws which the list would clearly include have been violated on a mass scale, in which case SVLK certification would not suffice to meet due diligence requirements. One observer points out that most timber concessions, as of 2004, had not properly completed the required gazetting process, whereby forest areas are

² Annex 2 of the SVLK Regulation provides that field checks are required to confirm: (1) the absence of harvesting from exclusion zones; (2) the actual boundaries of felling blocks as compared with approved boundaries; (3) that harvesting equipment complies with their permits; and (4) that environmental impact assessments and associated documents are being properly implemented.

classified, delimited, and officially registered (Colchester 2004). Concessions are “frequently” granted to entities that lack proper qualifications, and forest clearing is commonly done using fire, which is doubly illegal when done in deep peat soil (Prasetyo *et al.* 2012). Processed wood coming out of a number of large plywood mills may be illegal since mill owners ignored a Ministry of Forestry order that they cease operations due to indebtedness (Ibid). Zealous regulators and nervous operators might view such violations as a basis for severely curtailing trade in Indonesian timber.

CONCLUSION

Concerns about the robustness of the SVLK are serious. Indonesia's timber sector may be too complex to permit effective legality verification of all harvesters and processors, and even if it were not, there is a dearth of qualified, impartial experts to serve as auditors. Those auditors that are available face improper incentives to please both the companies that hire them and the government that assists them, and even rigorous auditing may be insufficient to ensure meaningful environmental and social management given weak legal requirements. Further, the SVLK may concentrate too much power in the hands of the auditors, provide for too little outside monitoring to ensure that auditors do not abuse their power, and jeopardize the ability of small-scale timber enterprises to compete with larger operators.

There are measures that the Indonesian government could take to address some of these concerns. To increase the number of qualified and independent auditors it could increase the resources available for training and set up a semi-autonomous or non-governmental body to provide them with technical and financial assistance. To give audits more teeth, it could impose stricter legal requirements for proper environmental and social management of timber operations. Greater authority for external actors to monitor the auditing process would both ensure more robust audits and incorporate greater public participation in the legality verification process. Subsidies for small-scale operators to go through the SVLK permitting process may be needed for some time to ensure that capital constraints do not disadvantage their ability to access the export market.

Whether or not the challenges associated with the SVLK are addressed, concerns for its robustness are now moot as far as Indonesian timber exports to Europe are concerned. The SVLK has become the sole instrument for assuring the legality of Indonesian timber under the VPA. The VPA has displaced the EUTR as the rulebook governing Indonesian timber exported directly to the EU, and the SVLK's design is safe from critique, pending final approval by both the EU and Indonesia (although monitoring mechanisms will still ensure that it functions properly going forward). The EU has negotiated the terms of the VPA, and must either live with any weaknesses that it failed to address earlier, or risk backtracking from what has been accomplished.

This does not, however, render the EUTR useless with respect to Indonesian timber. An uncertain, but probably

significant percentage of Indonesia's timber is likely to reach Europe through third countries, especially major markets in the Asia-Pacific region. The VPA does not cover this segment of the market, meaning that the EUTR still serves to screen out illegal products exported from these countries which originate in Indonesia. Consequently, with respect to these indirect exports, the SVLK downgrades from constituting sure proof of legality to merely being one of a number of factors for EU regulators to consider when determining if operators have satisfied their due diligence obligations. Moreover, there is a strong argument that operators and regulators need not (and in fact cannot) view certificates demonstrating SVLK compliance as sufficient to meet due diligence requirements. First, the SVLK probably cannot produce certification that would constitute valid “assurance of compliance” because it most likely does not meet the criteria elaborated in the clarifying regulation concerning due diligence for a certification scheme to lend confidence that timber is legal. Moreover, as the “assurance of compliance” afforded by certification is only one of several risk assessment criteria to be considered—and one that is not even mandatory—the EUTR probably does not conceive of third-party verification schemes in general as being sufficient to satisfy due diligence obligations. As a result, operators may have to demonstrate proof of legality beyond that afforded by SVLK certification for a significant portion of Indonesian timber entering the EU. This could prove a boon to advocates for strong action against illegal logging given the possibility of continued wide-scale illegality in Indonesia's forest sector.

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