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SOURCING TIMBER FROM BRAZIL

Risk Mapping and Mitigation

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CONTENTS

1 INTRODUCTION

The note is aimed at Danish companies that purchase or consider purchasing timber from Brazil or that for other reasons are exposed to sustainability risks related to the Brazilian timber supply chain.

The objective is to map the current landscape of risk and mitigation strategies in Brazil. As such, the emphasis is on issues still outstanding, which should in no way belittle the many achievements already made, the great majority of compliant and sustainable producers in Brazil, nor the positive prospects and ambitions of the new Brazilian administration. Indeed, the hope of the authors is that this report will give insights into the many promising risk mitigation initiatives and building blocks already available in Brazil. The note is thus meant to supplement and bring these together with potential risk areas in the timber supply chain being the mere starting point for the forward-looking analysis.

Brazil has the second largest area of forest in the world at nearly 500 million hectares (59 % of its territory) of both natural and planted forests. Natural forests occupy around 485 million hectares in Brazil or 98 % of the forest area. The majority of this forest is in the Amazon biome with the two states of Pará and Mato Grosso supplying 70 % of Brazil's tropical timber[1]. According to an impact assessment of the European Commission, underpinning its proposal for a deforestation due diligence regulation, 9 % of the timber imported to the EU from 2015-2019 came from Brazil[2].

The imports from Brazil to Denmark in 2021 of the four biggest wood goods groups[3] (as classified by the EU combined nomenclature) totaled 187.1 million DKK. Another four minor wood groups[4] add 7 million for a total of 194.1 million DKK or a total 10.97 % of Danish imports from Brazil in 2021. These imports will be covered by the EU regulation on deforestation-free products as proposed by the European Commission.

2 ENVIRONMENTAL ASPECTS: AN OVERVIEW OF THE CHALLENGES

Timber production in Brazil has been associated with a number of environmental problems[5]. Recent studies analyzing more than 300 Federal

[1] P.6 FT4392_BrazilDash_July_2021.indd (forest-trends.org)

[2] EUR-Lex - 52021SC0327 - EN - EUR-Lex (europa.eu) p. 60.

[3] Consisting of the following HS-codes: **HS-4401:** Fuel wood, in logs, billets, twigs, faggots or similar forms; wood in chips or particles (67.4 million DKK), **HS-4407:** Tropical wood sawn or chipped lengthwise (31.5 million DKK), **HS-4409:** Wood, incl. strips and friezes for parquet flooring (14.6 million DKK) and **HS-4412:** Plywood, veneered panel and similar laminated
wood (73.6 million DKK).

[4] Consisting of the following HS-codes: **HS-4411:** Fibreboard of wood or other ligneous materials, **HS-940340**: Wooden furniture for kitchens, **HS-940350:** Wooden furniture for bedrooms, **HS-940360:** Wooden furniture.

[5] For an overview, cf. for instance: FT4392_BrazilDash_July_2021.indd (forest-trends.org)

Police operations between 2016 and 2021, have confirmed that illicit practices are found in different stages throughout the timber supply chain[6]. Besides the selective logging permits, it could be unauthorized transport and sale of wood, including protected species. Finally, illegalities may concern fraud in land titling and licensing documents through change of species and type of material or volume. By mapping said operations, the study found that a subsystem of illegal logging exists in several municipalities, mainly in Maranhão, Rondônia and Pará, including Amarante do Maranhão (Maranhão), Ji-Paraná, Cacoal and Porto Velho (Rondônia), Altamira and Anapu (Pará)[7].

Another initiative called Simex by a network of reputable Brazilian NGO's has mapped the exploitation of timber in seven of the nine states in the Amazon region[8]. 377,624 hectares of timber exploitation covering the period August 2020 to July 2021 was mapped based on official data. Only 62 percent of this area was exploited in conformity with valid logging licenses indicating widespread legality issues.

Of the non-authorized exploitation, 72 percent took place on private land and 11 percent on indigenous territory. The study maps the municipalities as well as the protected areas (indigenous territories and nature conservation areas) most exposed to unauthorized timber exploitation in the period concerned (see links in note 10 for details).

The problem is quite concentrated: 100 private properties represent just over half of the area exploited without authorization in this category. Ten protected areas represent 80 percent of the total non-authorized area in this category. Only ten municipalities concentrate almost half the total area exploited without authorization. However, comparing the ten municipalities with most legal and illegal exploitation, five municipalities coincide/appear on both lists.

The places mentioned in the above studies are not the only ones in the Amazon with risks associated. In general, one cannot rely on geographical criteria alone for illegal timber control, but needs to adopt a supply chain based approach.

Reinforcing this need, the EU Timber Regulation and the proposed EU due diligence regulation on deforestation require that importers in the EU implement a due diligence system to ensure that they do not import timber that has been illegally harvested respectively and has not contributed to deforestation or forest degradation after a certain cutoff date. In order to meet these requirements, the EU Operators need access to certain information about the supply of timber, and assess and mitigate risks.

[6] The-ecosystem-of-environmental-crime-in-the-Amazon.pdf (igarape.org.br), p. 11.
[7] 2022-07-AE-territories-and-trajectories-of-environmental-crime-brazilian-amazon.pdf (igarape.org.br), p. 20. See also pp. 24-27 dedicated to timber and pp. 44-48 mapping arcs of forest destruction.
[8] Full study: Boletim_SIMEX_AMZ_2021.pdf (imazon.org.br)

On this background, this note maps selected risks related to sourcing of timber from Brazil and set out some pointers for dealing with these risks, while providing specific due diligence tips. As such, it does not claim to cover all aspects of responsible sourcing from Brazil.

Important note: both market and legislative status, expectations and requirements are evolving dynamically. This report constitutes no official recommendation, approval or indication of any mitigation measure's compliance therewith. It represents best efforts but does not substitute companies' own due diligence duties and does not claim to be complete, exact and up-to-date in all respects. The Danish Ministry of Foreign Affairs cannot be held liable for its use, which is merely meant as a starting point and guide of inspiration. The Trade Council (part of the Danish diplomatic mission in São Paulo) is, however, available to help Danish importers update or develop their current due diligence strategy for timber import from Brazil – please refer to section 4 for our contact details.

3 DUE DILIGENCE STRATEGIES

An good starting point, when considering procuring timber from Brazil, is the guide published by Preferred by Nature and financed by Danida. The guide gives an overview of sources of legal timber and a risk assessment overview of main issues to watch out for. Both the risk assessment summary and the mitigation recommendations, including on-site verifications, can be a useful starting point for defining a procurement protocol, depending on timber source types and the different legislation that applies for these types[9].

CERTIFICATION

The most obvious mitigation strategy is to buy only certified material. Currently, several certifications are available when trying to source sustainable timber from Brazil.

It is important to note that although certified material may play a role in the due diligence process, it is not an automatic "green lane" to meet the due diligence obligations of the EU Timber Regulation (EUTR) and in the future the EU deforestation due diligence regulation. However, even though the schemes are no guaranteed green lane they still provide safeguards that support legal trade in timber products, and they ensure a higher degree of assurance for sourcing companies compared to non-certified material or supply chains.

A specific study covering a range of certification and verification schemes in the forest sector and for wood based products was elaborated to support the impact assessment accompanying the Commission's proposal for a due diligence regulation. The study concluded that none of these schemes *"are perfect or can provide complete control of*

[9] Brazil | Preferred by Nature | global, page 3:
- Timber from national forest; both on state and privately owned land.
- Plantation forest (timber, both native and exotic species from plantation forests on privately owned land.

supply chains, but at the same time they are an essential tool to meet the EUTR requirements[10]".

Additionally, the study found that "*the risk of fraud, e.g., in supply chains is generally poorly covered. There seems to be no approach to enable auditors to detect and act on fraudulent practices by forest managers or in the supply chain[11]".*

Another significant finding of the study is a key gap in regards to the traditional model of chain of custody (CoC) systems to track the claims of certification from the forest to the final buyer. While the traditional CoC systems do provide a systematic approach to transferring claims throughout the supply chain "*they do not include the systematic ability to verify transactions of volumes, species and qualities between entities, which leaves the system vulnerable to manipulation and fraud*"[12].

It is important to underline that said study evaluates a number of certification schemes such as the FSC (Forest Stewardship Council), the SBP (Sustainable Biomass Program) and The Programme for Endorsement of Forest Certification (PEFC), but not only. The study shows that "*there can be significant differences in what certification schemes cover, how they operate and how well they address risks of illegal harvesting and trade in certified supply chains"[13].*

As such, the study can act as a direct support to your risk assessment by providing information on where potential strengths as well as gaps may exist in the coverage of the specific certification scheme[14]. Strengths and weaknesses need to be considered when buying certified materials and may vary from country to country. Be aware that the benchmark used by the study for the evaluations of certification schemes is the EU Timber Regulation (EUTR). The deforestation due diligence proposal by the Commission goes further in some respects by making a specific link to deforestation with geo-localization requirements.

ON THE IMPORTANCE OF THIRD PARTY FIELD AUDITS

The risk summary and mitigation recommendations set out by Preferred by Nature, cf. above, deals with certain geographic aspects such as mapping traditional communities in wood-supplying districts and conservation units in the vicinity of wood supplier districts.

[10] Study on certification and verification schemes in the forest sector and for wood-based products - Publications Office of the EU (europa.eu) page 6

[11] Ibid. page 6

[12] Ibid. page 6

[13] Ibid. page 6

[14] The study can be a bit overwhelming at first sight. Pages 56-60 provide a useful summary and overview in table form of the certification schemes assessed by the study. The following five chapters are dedicated to further analysis of one certification scheme each, cf. table of contents. Pages 150-52 contain useful advice, when applying due diligence to certified wood products.

The importance hereof is underlined by a comprehensive investigation by Greenpeace covering all valid logging authorizations from 2016-2019 in the state of Pará that contained species of Ipé[15]. The investigation showed a spatial concentration of forest management plans with (unrealistically) high and very high Ipé densities near protected areas, indigenous lands and rural settlement areas (acting as an indicator that such high densities are used to receive logging credits for the harvesting and movement of timber, which could in fact well come not from the area of the plan, but instead illegally from those neighboring protected areas).

The investigation concludes that considering the chronic problems affecting the licensing, monitoring and inspection of Brazil's timber sector, evaluation of documents issued by government bodies are not sufficient for guaranteeing legality. It therefore recommends that importers use and publish third party field audits carried out by individuals, organizations or companies with appropriate knowledge of the industry and its practices to catch implausible document claims.

Isotope testing is another evolving physical inspection tool that can assist companies in carrying out due diligence. By verifying the origin of timber, isotope testing can provide supporting evidence by supplementing the mainly paper-based chain-of-custody documentation and be a way to deal with fraud in the supply chain.

OTHER DUE DILIGENCE TOOLS

BV Rio has published a widely acknowledged due diligence and risk assessment tool based on large databases and satellite imagery. The system uses a Big Data approach, collecting and analyzing information about legality (including the risks of non-compliance with environmental and social requirements in harvesting, processing and transportation stages), inconsistencies in the market chain and other environmental and social aspects (such as embargoes or violations of labor legislation). The tool flags transaction with larger legality risks on the basis of official documents. As such, it is not a substitute for the importance of field auditing, cf. above.

Another interesting new due diligence tool is Timberflow, which is being developed by Imaflora. The tool allows you to enter the CNPJ (Brazilian Registry of Corporations) of your exporters into the system and from there see the most likely supply chain of your timber and the likely area of origin, while ranking the municipalities based on the risks connected to sourcing from these. Timberflow will additionally show the exportation routes of the timber and species based flows.

Timberflow will - based on the entered CPNJ number - be able to show if the company has any current or previous embargoes from IBAMA (Brazilian Institute of the Environment and Renewable Natural Resources) and show potential connections to slave and child labor. The intention is for Timberflow to provide information about deforestation,

[15] Ipé is a valuable tree species used for flooring and decking.

degradation and other indicators at the municipality level to be used by market operators to exercise their own due diligence judgment as to choosing suppliers in regions less affected by/with smaller risks of deforestation, degradation, and potential poaching of protected areas[16].

A final company that does certification and assessment services is SysFlor. SysFlor provides services including certification of forest management of both plantations and native forests according to the Brazilian Forest Certification Program (Cerflor) and the performance of Independent Forest Audits – AFI – to national and state forest concessions.

4 LOOKING AHEAD

Mitigating risk while sourcing timber from Brazil is complex not least due to the risk of fraud and contamination along the supply chain. Even geolocalization does not guarantee against "timber washing", such as misusing exaggerated volumes in an authorization or exaggerated conversion rates from logs to saw wood at sawmills to launder illegal timber.

In general, the risk of fraud makes it imprudent to rely on a paper-based approach alone. On this background, several layers to a reasonable mitigation of risk while sourcing wood from Brazil can be identified:

- First, it would seem prudent to consider to simply avoid a few high risk zones, say, in close proximity to the protected areas most at risk from illegal logging[17].
- Second, sourcing only certified wood will by virtue of chain of custody allow you some level of controls of e.g., conversion rates at sawmills.
- Third, operating with a simple/short supply chain to minimize potential sources of contamination, for example a concession with its own sawmill. This in itself will make it easier for a geographic information system professional to run cross-checks of official databases of farms/forest exploitation areas with satellite-based monitoring of deforestation[18].
- Fourth, if your sawmill supplier has a more complex web of suppliers, it seems prudent to require that the mill has undergone a chain of custody certification with period audits.

[16] It is worth noting that Timberflow is for native species - it will not cover timber sourced from plantations. The tool is expected to be launched and available online for free within the next 6 months.

[17] cf. the Simex study mentioned in section 1 above (consider approaching its authors) and Timberflow.

[18] Official databases exist under the aegis of INCRA or the official environmental cadastre called CAR. Geo-monitoring can be done through the Prodes geomonitoring programme of the Brazilian space agency, INPE.

- Fifth, technological and paper-based regulatory systems are developing at a rapid pace and will decrease contamination risk but still seem no substitute for “good old-fashioned” independent third party field audits along the chain. To mention some examples: DNA-based traceability instruments are being developed, but will not solve fraud if they only test at local storage sheds, where timber of different origin is collected. Isotope testing depends on the size of its “catalogue of samples” that you compare the tested wood against in order to be precise enough.

5 OUR CONTACTS

The Trade Council in Brazil stands ready to help companies and institutions with an interest in understanding sustainability risks related to the Brazilian timber sector. We can help you reach out to relevant partners but also assist on ground with concrete due diligence activities based on our many years of experience and vast local network within sustainable value chains.

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ANNEX 1: FEDERAL TRACEABILITY REQUIREMENTS

An understanding of Brazilian Federal documentation requirements also presents a way of avoiding some of the potential risks of fraud associated with Brazilian timber products. A way to avoid some risk of fraud could be to ask export partners/traders to see proof of the existence (online registration) of the following documents: SINAFLOR/SINAFLOR+ and DOF.

Origin controls and legal transactions for timber and by-products of native species from natural and planted forests are conducted using SINAFLOR, which in turn is integrated in the DOF (Document of Forest Origin), and similar state systems[19]. Together these documents constitute the Brazilian federal forest management system (see Annex 1) and according to IBAMA, ensure traceability of the timber from origin to export. Trade in timber and native species can only be conducted with an Export DOF or a similar state document.

Especially the DOF, which constitutes the license that allows timber and by-products or native species from natural or planted forest to be legally exported, is known to be surrounded by significant risk.

IBAMA'S website offers a way to check the credibility of a DOF document. Here it is possible to check a DOF number and compare the provided data on the site with the information provided by the SINAFLOR/SINAFLOR+ system: type of timber, location of forest, transportation routes etc. If there are discrepancies between the DOF and the SINAFLOR+ system, there is a risk that you have been given a wrong/fraudulent DOF certificate and thus the overall risk of sourcing illegal timber increases[20].

IBAMA has recently launched a new version of DOF called DOF + traceability, which will gradually replace the original DOF. DOF+ traceability will be integrated in Sinaflor+ and will permit traceability of logging permits throughout the supply chain by means of a code.

In addition, IBAMA is currently developing Brazil's Single Authorization Platform[21] (Plataforma de Autorização Única do Brasil - PAU-Brasil). Through this platform, all activities pertaining to trade in products and by-products of Brazilian biodiversity will be assessed and submitted to risk management analysis before a SISCOMEX - a system that manages customs operations in Brazil - license can be issued.

[19] Mato Grosso and Pará have their own DOF system called **Sisflora** and Minas Gerais use **SIAM,** both systems controlled by IBAMA (Ibama is the Brazilian environmental supervision, monitoring and control agency).

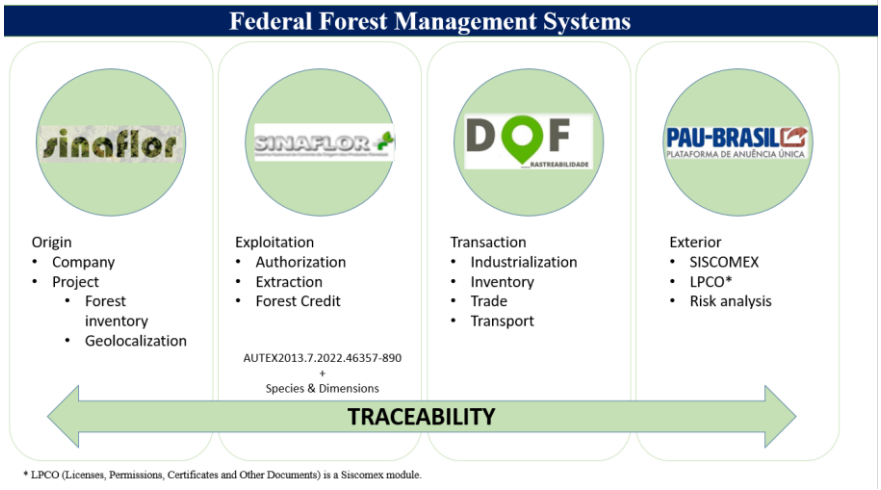
[20] For more information about Brazilian requirements for timber export see: Directorate for the Sustainable use of Biodiversity and Forests: 20210531Technical-Note042020.pdf (www.gov.br)

[21] 20210531TechnicalNote042020.pdf (www.gov.br) p. 14

PAU-Brasil is expected to be a handy single entry point connected to DOF+ traceability. This is expected to facilitate cross-checks of official databases of farms/forest exploitation areas with satellite-based monitoring of deforestation but will not by itself guarantee against fraud in the supply chain. It is not known when PAU-Brasil will be launched.

FEDERAL FOREST MANAGEMENT SYSTEMS

Below is an overview of the Brazilian Federal Forest Management System and the needed documents for exportation:



The Trade Council is part of the Ministry of Foreign Affairs. We advise Danish companies in export, internationalization and innovation as well as foreign companies that want to establish themselves in Denmark. With a presence in more than 70 countries, where we are represented at embassies, consulates general, trade offices and innovation centres, we have a close collaboration with the business world and a strong knowledge of local markets.

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