

## **Traceability and Regulation September 2024**

### **Navigating EUDR Compliance: How am I supposed to manage this?**

The upcoming European Union Deforestation Regulation (EUDR) has sparked significant discussion within industries importing products like cocoa, coffee, and timber into the EU. To gain a clearer understanding of the regulation and its implications, we sat down with Nicko Debenham to explore the challenges and responsibilities that businesses will face as the EUDR comes into effect.

---

**Robin: So apparently, I need to be ready for the EUDR. I'm importing cocoa products to the EU. How does this affect me?**

Nicko: Yes, you do need to be ready. The regulation is designed to prevent deforestation and applies to seven key products: cocoa, coffee, timber, cattle, rubber, soy, and palm. Under the key clauses—3a and 3b—you must prove that the farm plots where these products are grown have not caused deforestation since December 2020 and were not grown illegally. Every parcel shipped to the EU will need to be traceable to the farm plot, and you'll be required to conduct due diligence to ensure no or negligible risk. This involves data collection, risk assessment, and risk mitigation.

**Robin: Can't I just rely on my suppliers? I've been using them for years.**

Nicko: If you're the operator, meaning the person importing the product into the EU—what the regulation terms "placing on the market"—you're the liable party. You can rely on your suppliers, but only if you're certain they're meeting the regulatory requirements on your behalf. Essentially, you need to ensure that they are conducting due diligence to the standards required by the EUDR.

**Robin: What exactly are these protocols?**

Nicko: The regulation outlines specific protocols in Articles 9, 10, and 11. You'll need to collect data, assess risks, and mitigate those risks if they're identified. You must be able to trace each parcel back to the farm plot it came from to prove that no deforestation or illegal practices have occurred. This isn't just about having traceability; it's about ensuring that every action aligns with the plot of land associated with each shipment.

**Robin: Do you know any suppliers who are already compliant?**

Nicko: In the cocoa industry, roughly 50% of supply is direct, up from 40% before the EUDR started getting attention. These direct supplies are often certified through programmes like Rainforest Alliance, Fairtrade, or company initiatives like Cocoa Life and Cocoa Plan. However, not all of that supply is available for Europe—some goes to other markets like the U.S. Let's say 15% goes to the US, which means that you've got 35% to go to Europe, and 60% of the global crop needs to cross the EU customs border. The 35% will be ready. The big challenge is the remaining 25%, which comes from third-party, indirect suppliers. Compliance in that segment is still a major question mark.

**Robin: What happens if I can't establish proper protocols for that 25% of my supply? Have people dealt with that?**

Nicko: Definitely not. Many companies are currently struggling with this issue. Some supply chains are proactive, working with partners to establish data collection and traceability systems, while others are largely ignoring the problem. The progressive companies are classifying their suppliers into categories—red, amber, and green—based on their readiness; red being they just don't care and aren't interested, amber being they are interested but don't have a clue what to do and need help, and green being they're ready. If you can't ensure compliance, you'll need to find new suppliers or risk non-compliance yourself.

**Robin: Can warehousekeepers help with this process?**

Nicko: You are the operator, so you are the liable party. Your warehousekeeper is the custodian of your goods and therefore can sort out the traceability whilst they are the custodian of those goods. They can maintain traceability from the point they receive the goods, ensuring parcels are kept segregated and that related data stays with them. However, they can't establish if those parcels were originally compliant with the deforestation and legality clauses—those checks need to be done before the goods reach the warehouse.

**Robin: So, I'm thinking about the process where lots are formed by the Exchange, and they can be made up of more than one parcel. Presumably, these parcels need to be compliant before they can be combined. Once they're grouped together, are they just treated as a bulk parcel?**

Nicko: Let's say you have two shipments of 25 tonnes each, so you end up with 50 tonnes that you want to divide into five 10-tonne lots. If you can maintain the separation of those two original parcels, apart from one lot that might mix them, then two of the lots would carry the data linked to Bill of Lading A, two lots with Bill of Lading B, and one lot would carry data from both A and B. The key here is that you can only aggregate parcels—you cannot disaggregate them once they've been combined. If you cannot ensure that the lots have maintained their separation, then all five lots must carry the combined data from A and B. In other words, once parcels are mixed, the traceability must reflect that aggregation. The only way to disaggregate them would be if you had bag-by-bag traceability down to the individual farmer, but let's be honest, in the cocoa industry, that level of detail is practically impossible.

**Robin: What if I'm importing cocoa butter from Asian factories? Isn't that safe?**

Nicko: Even Asian factories need to prove that the cocoa they process has not violated the deforestation clauses. They need to maintain that to the satisfaction of any potential inspection by the National Competent Authority (NCA), dependent on where the finished or semi-finished product is shipped to within the European Union. So, they must maintain traceability from the Bill of Lading to the European Union, right the way to the farm plot where the cocoa was sourced from.

**Robin: Suppose I'm based in the UK, and I import cocoa butter from Singapore to later export to the EU. How does that work?**

Nicko: I wouldn't buy from you as a UK trader if they hadn't pre-established that. As a UK trader, you're just another leg in the same chain as the previous question.

**Robin: So, the Singapore exporter can expect a potential visit from the EU on goods that they didn't know were going to the EU?**

Nicko: Correct. If an NCA does a detailed inspection on a specific parcel, they might ask for traceability evidence that aligns with the regulations. Let's say the supply chain starts in Africa, moves to Asia, and the goods transform Harmonized System (HS) codes several times before arriving in Europe. The operator must be able to demonstrate that every step is compliant and that there's no risk of contamination in the supply chain. The NCA has the authority to demand this evidence, although whether they'll actually do it is another matter. If they find that there isn't enough evidence to show due diligence, they can fine the operator. It's based on a reversal of the burden of proof, meaning the operator is presumed guilty until they can prove otherwise. So, the NCA could say, "You haven't provided enough evidence; here's a fine. You can appeal, but you'll need to provide much more proof than you initially did."

**Robin: This sounds like a nightmare. I didn't realise that people could be trading cocoa innocently, and suddenly they find the EU turning up at their doorstep.**

Nicko: Exactly. Imagine if an Asian factory refused to cooperate with an NCA—saying, "Who are you? Go away!" The NCA would go back to the operator in Europe and say, "You haven't done your due diligence, so here's a fine." The responsibility and liability are entirely on the operator. If you're an operator buying from a UK shipper, you must demand data showing where those parcels came from, down to the cocoa's origin. If the shipper can't provide that information, you should refuse to buy the parcel. If you proceed without this data, you're essentially shooting yourself in the foot.

**Robin: What if I don't know if the cocoa will end up in the EU?**

Nicko: Even if you're unsure, you still have to do your due diligence. If the product ends up in the UK but you don't know where it originally came from, it cannot be re-exported to Europe. If there's any chance it could go to Europe, you must assume it might and do your due diligence accordingly.

**Robin: So, even if I don't know where the cocoa will eventually go, I still need to ensure compliance?**

Nicko: Yes. You have to operate under the assumption that it could end up in Europe. If you're confident it won't, then don't worry. But if there's even a slight possibility, due diligence is non-negotiable. Any buyer in Europe will demand proof that the cocoa plots are compliant, showing no or negligible risk of illegal activity. They'll ask for that data—or they'll want ICE CoT to validate it for them.

**Robin: Can I rely solely on ICE CoT to ensure compliance?**

Nicko: You can rely on ICE CoT to validate compliance with key regulations like Articles 3a and 3b, but the data still needs to come from your suppliers. ICE CoT doesn't collect data; it validates it. The actual collection and traceability have to be done by your suppliers. ICE CoT then assesses that data and provides validation.

**Robin: So, if the data is on ICE CoT, can I assume it's been properly validated?**

Nicko: There's no guarantee but using ICE CoT gives you a very high level of confidence that the risk of non-compliance is negligible.

**Robin: If I decide to only buy cocoa on ICE CoT, do I still need to do anything else?**

Nicko: Essentially, ICE CoT would be doing your due diligence for you. They won't issue a guarantee, but they'll validate that the data is compliant. They assess whether the plots have caused deforestation, if they're in protected areas, or if other illegalities are involved. However, if someone deliberately fabricates data, ICE CoT can't protect you against that.

**Robin: That's fair enough. But if I wanted to have a shortcut, then ICE CoT would go 90% towards that.**

Nicko: If you're buying from a third-party shipper or managing your own supply chain, you can use ICE CoT to validate farm plots, identify risks, and address any critical issues. They'll flag anything non-compliant, which you can then mitigate or exclude from your supply chain. There are these degrees of conformity, which are then categorised between critical and non-critical. The critical ones cannot be accepted unless you manage to mitigate the reason why they are critical, and in some cases, it would be impossible because they have caused deforestation.

**Robin: How can I do due diligence when I don't know what I'm going to be declared?**

Nicko: That's where supply chain management becomes critical. You need to have assessed your suppliers' readiness long before shipment. If you haven't done that by now, you're probably in trouble. You need access to the data before approving any shipment. That data should include farm plot locations, evidence of compliance with deforestation regulations, and proof that risks of illegal activity have been mitigated. Then, you tell the shipper, "Log the data on ICE CoT; I'll review it, and if everything checks out, I'll approve the shipment." Once it's been approved you say, "Once you've shipped it, you need to send me the Bill of Lading, and a copy of the waybill from the aggregator to your warehouse at portside prior to the Bill of Lading." By doing that, you've established no, or negligible risk of deforestation or other forms of illegality and you have evidence that it did come from the aggregator that has that list of farm plots.

**Robin: So, I'm just thinking about our contracts. The standard contract doesn't go back further than the declaration, so parties need to establish before shipment that the parcel is compliant.**

Nicko: Technically, you don't have to, but if you don't establish compliance before shipment, you risk having the entire parcel rejected. No one will pay you unless you establish no, or negligible risk of Articles 3a or 3b. Your parcel becomes worth zero. It's not like a weight or quality problem or it's a bit late in the backward-dated market. This is a different ballgame. If even a small part of the shipment is non-compliant, the whole parcel becomes worthless. That's why, under contract terms, you need to establish that trigger point—shipment approval. The contract should clearly state that the shipment is at the shipper's risk until approval is granted.

**Robin: So, you can't buy CIF?**

Nicko: You can, but shipment only after approval, which only comes after assessing the data linked to that shipment.

**Robin: What if you have a parcel afloat and want to sell it to me, but I can't buy CIF because I have no idea what was agreed upon initially?**

Nicko: If you ship and have a parcel afloat as a shipper, the liability rests with you. If you're an operator, you'd need the data, waybills and Bills of Lading before accepting the shipment. If it turns out to be non-compliant, you should return ownership to the shipper and still hold them responsible for delivering compliant cocoa.

**Robin: On the contract clauses I sent you there was no mention of any consequence for non-compliance.**

Nicko: That's the key point. If the cocoa is found to be non-compliant, what are the consequences? The shipper remains the owner and must replace it with compliant cocoa. The contract needs to clearly state these consequences.

**Robin: So, there will be a consequence of non-compliance. But I'm concerned about the pre-shipment part of it that we haven't addressed, but in a way, we have. I've said that we need to establish what platforms are acceptable. Once you comply with that platform and it is acceptable, then you're free to make the declaration and provide the data.**

Nicko: Under any contract, there needs to be a clear trigger point where liability shifts from the shipper to the buyer. In my view, that trigger is shipment approval. How you decide to give shipment approval is up to you. For instance, if you're an operator, you could send an email saying, "We have a 100-tonne contract, you've sent me the data, it's on ICE CoT, and I've reviewed it. I'm satisfied, and I officially approve the shipment." At that point, liability moves from the shipper to the operator. In a detailed contract clause, you might specify that an operator could use ICE CoT or another platform for this approval process. However, some might choose to handle it internally.

**Robin: I can see that what's missing is the acceptance of the declaration, so something needs to be in the contract terms regarding the acceptance of the declaration.**

Nicko: Just be careful with that. Accepting a declaration could imply that it's okay to ship before you've received approval from your buyer. Essentially, a declaration signals that the goods are already on the ship, which is a risky approach. Ideally, you shouldn't ship at all until the buyer has fully reviewed the data and confirmed they're happy for you to proceed with the shipment.

**Robin: Let's say I'm the buyer, and you've provided the data, which I'm fine with. You now want to sell to me on a CIF basis.**

Nicko: In that case, I've sold you 100 tonnes, but you don't want it shipped until you've completed your EUDR checks. You'd ask me to upload the data to ICE CoT and release it to you. You might come back and express concerns about one parcel, possibly due to deforestation issues. At that point, it's my responsibility to prove whether it meets compliance standards. If it doesn't, it gets excluded from the shipment. I would then provide additional evidence—maybe showing that the deforestation occurred before 2020—and once you're satisfied, you'd approve the shipment. That's how the process should work. Then, the shipment can proceed. If you don't receive copies of the waybills with the original Bill of Lading, you're within your rights to refuse payment. The waybill is critical because, without it, you can't prove that it came from the specified aggregator and the related farm plots thus proving compliance to the NCA, leaving you vulnerable to fines of the value of the parcel and in extreme cases of up to 4% of your turnover in the EU.

**Robin: So, you need to specify that in your contract. It's an additional document.**

Nicko: Exactly. One of the current challenges is the lack of clear guidance from the European Commission. The FAQs and guidelines haven't been fully updated, which makes it difficult for operators to include specific clauses. The practice of asking for copies of waybills with the original Bill of Lading, this requirement isn't officially listed in the Commission's documentation. We've received this information verbally from the competent authorities, who have indicated that they want to see waybills tracking the journey from the farmer-facing aggregator to the port, along with the Bill of Lading for traceability.

**Robin: There's bound to be a difference. If they're expecting numbers to match up, they won't.**

Nicko: Right, but here's what a major member state competent authority explained to me. To confirm that a Bill of Lading corresponds to specific farm plots, they'll need to trace it back through the operator's system. This means identifying which aggregator the shipment came from, gathering evidence from that aggregator, and then cross-referencing the list of farm plots they have. They'll compare those plots with the information on the due diligence statement linked to the Bill of Lading. If they find any farm plot listed that doesn't match the aggregator's data, it's a red flag—it indicates the cocoa came from a different source. During their annual inspections, they'll aim to cover around 9% of shipments. As part of this, they'll randomly select parcels for deeper investigation, where they'll check the due diligence in

your system, including the aggregator's details, waybills, and farm plot lists. If any farm plot doesn't align with the aggregator, you'll need to provide proof that the plot is legitimate. It's a straightforward but very granular process.

**Robin: Well, I hope we'll have the documents available. Certainly, on the list of documents, what needs to be included are the weight notes. You know, a CIF parcel needs a bill of lading, insurance certificate, invoice, freight-paid bills of lading, and now weight notes.**

Nicko: The issue we're facing is that until the FAQs or a formal statement from a competent authority comes out, there's a lot of uncertainty. The consensus is that it's not possible. It's entirely possible and it's going to be required by the competent authorities. The challenge is that the Commission hasn't released those FAQs or guidelines yet, which is causing hesitation.

**Robin: Logic suggests that's the direction they'll take.**

Nicko: Exactly. They know it's unrealistic to trace everything down to the exact farm plot, so they'll focus on the aggregator level because that's manageable. During an inspection of their system, operators will need to show that the farm plots within the aggregator match what's on the bill of lading. If they can't align those details, then there's a problem. It's as simple as that.

**Robin: Couldn't shipping companies take on some of this responsibility? After all, they're the ones accepting the goods for shipment—they shouldn't take goods that are illegal to be imported.**

Nicko: Shipping companies aren't liable in this context, just like they aren't responsible for quality or weight loss issues. They limit their liability to ensuring that the cocoa loaded onto their ship is delivered as expected at the destination. While they can confirm that it's your cocoa on board, they're not responsible for verifying compliance. That due diligence has to be done before the goods are handed over to the shipping company.

**Robin: Who is considered to be an operator?**

Nicko: You're classified as an operator if you place the product on the EU market or in any EU member state market. In other words, anyone bringing product across the EU customs border is considered an operator.

**Robin: If I export cocoa to the EU and it goes into bond, I actually haven't entered the EU, have I?**

Nicko: No, and therefore you're not in scope for EUDR yet.

**Robin: So, if I stick to that, I'm not liable?**

Nicko: No, if you then re-export without crossing the customs border, you are not liable.

**Robin:** So, if I wish to sell that cocoa, I have to show to my buyer, who perhaps wants to take it into the EU, that everything is compliant. Even if I'm not an operator, I still have to show that that cocoa is compliant in order for my buyer to bring it into the EU.

Nicko: Yes, if it's sitting in bond, it's not within scope because it hasn't been placed on the market yet. If your buyer plans to bring it into the EU, you will need to show that it's compliant.

**Robin:** So, anyone who thinks they can avoid compliance by just storing it in bond and running away isn't off the hook. They'll still have to prove that the cocoa is compliant, or else it becomes worthless, or you have to re-export it elsewhere.

Nicko: Exactly. They'd have to re-export it to somewhere that's not subject to EUDR.

**Robin:** What exactly do I need to show if I'm importing cocoa into the EU? What information is required?

Nicko: When importing, you need to establish the product type, the period when it was produced or harvested, the HS code, a description, the customs reference number, Bill of Lading details, and the geolocation data for all farm plots smaller than four hectares—or polygons for plots larger than that. All of this must be logged into the European Commission's information system. You also need to maintain a system proving that you've done the required due diligence and that your risk assessment shows negligible or no risk or that you have established mitigation to achieve negligible or no risk. During import, you'll need to upload those details to the system, and you'll be issued a due diligence statement. You pass this statement to your counterparty, and if you transform the cocoa into a different HS code (like butter, liquor, or chocolate), you'll need to issue a new due diligence statement by referencing the previous one.

**Robin:** Will the fact that the beans are on ICE CoT be enough for this?

Nicko: Yes, ICE CoT will allow you to transform the product (from beans to liquor, liquor to butter, and so on) and maintain the traceability needed to issue a new due diligence statement. Even if it's just beans, ICE CoT provides the data you need to upload to the information system and obtain the necessary due diligence documentation.

**Robin:** Do you think this whole process will be delayed?

Nicko: Personally, I doubt it. Even though there's talk of delays from certain political groups like the European People's Party (EPP), the Greens and the Left are against it. The problem as well is that any attempts to delay would probably take longer to finalise than the time it would take for the regulation to come into effect. The official application date is in December, so even if there's talk of a delay, it likely won't be implemented until March or April—by which time it will already be in application.

**Robin:** Will all the competent authorities from each member state act the same?

Nicko: They've said they're aligning under the same mechanisms they used for the European Union Timber Regulation (EUTR), but it's not guaranteed. If they don't align, it could create



serious problems. The Dutch authorities seem the most transparent, but we're still waiting for more clarity. The Belgians are holding a webinar on the 24<sup>th</sup> of October, just weeks before the regulation goes live, and hopefully, that will shed some light on whether they'll be aligned. If they aren't, it will be a nightmare for major players who operate across multiple countries. Discrepancies in enforcement could cause absolute chaos.

**Robin: The probability is that if they do, or even if there's a threat that they are not aligned then people will go for one particular port. If there's even a hint of misalignment, won't everyone just funnel shipments through the most lenient port?**

Nicko: Exactly. It would be an arbitrage situation. You'd see an excess of shipments to the lenient port with trucks queuing ready to move shipments across Europe.

**Robin: Once again, thank you for sharing your insights with us today. It's been a pleasure hearing your perspective. We appreciate you taking the time to join us and offer such valuable information.**