

New Environment Act demands more diligence in supply chains

Commercial analysis: The Environment Act 2021 (EA 2021) received royal assent on 9 November 2021, bringing into force new supply chain obligations for businesses to prevent deforestation. Anita Lloyd, director and Simon Garbett, partner at Squire Patton Boggs examine the new obligations and the part that lawyers can play in meeting these new responsibilities.

This analysis was first published on Lexis®PSL on 30 November 2021 and can be found [here](#) (subscription required).

What is the impact of Environment Act 2021 Schedule 17 on supply chain management?

EA 2021, s 16, Sch 17 aim to reduce deforestation caused by agriculture, by putting in place a framework for new requirements on business involved in the use of 'forest risk commodities'. Exactly what this term will mean is to be defined in later regulations, but the proposals for this legislation are linked to a government-commissioned report by the Global Resource Initiative, which identified seven key commodities:

- beef and leather
- cocoa
- palm oil
- pulp and paper
- rubber
- soya, and
- timber

Timber is already covered by a separate regime derived from the EU timber regulation, and EA 2021, Sch 17 specifically excludes the regulation of timber products (which would also include many paper products), but we can anticipate that this new regime is likely to cover the other commodities.

Affected businesses (operating in the UK and with turnover above a threshold to be specified) will be prohibited from using forest risk commodities in their UK activities if local laws (in the country of origin) were not complied with in relation to that commodity. Businesses must also establish and implement a due diligence system, identify and assess risk in relation to these commodities, and report annually in relation to that due diligence system.

Companies involved in supply chains which include forest risk commodities will have to establish that the commodities were not illegally harvested/produced by implementing a system of due diligence through their supply chains, back to the source of the relevant commodity. This is likely to involve additional information flow through supply chains, additional administrative steps in vetting new and existing suppliers, as well as ongoing management of the suppliers and collection of information.

More detailed requirements of the required due diligence system will be included in secondary legislation, but we can anticipate that these requirements may be similar to those required under the timber regime (which include access to detailed information about the product, where it is produced and details of local regulation, risk assessment and risk mitigation, as well as evaluation and continual improvement).

No announcements have been made yet regarding the timing of the secondary legislation, which will be needed to implement the framework established by the EA 2021.

Will this be effective/what more can be done?

The effectiveness of this latest regime aimed at ‘forest risk commodities’ will be very dependent on enforcement, as seen with the timber regulation. Recent ‘fitness’ checks on the EU timber regime have highlighted lack of and variability in enforcement, which has significantly hampered the potential for this due diligence based system to evolve and have a meaningful effect on imports of illegally sourced timber into the EU. It has also been criticised for ‘loopholes’ in its scope, which allow some products that are potentially affected by illegal logging to remain out of scope. But if lessons are learned from the implementation difficulties experienced with the timber regulation, there is the potential for these forest risk commodity provisions to be more effective, more quickly.

Initially, a number of trade associations representing leading food suppliers questioned the need for this legislation, and expressed concerns that it may harm supply chain resilience and drive up costs. However, more recently there have been calls from many stakeholders, including NGOs and large retailers, for the legislation to go further. The aspect that has been most widely critiqued is the reference to compliance with local laws, rather than with UK-imposed standards. The concern is that as many key supplier nations for these commodities may not have local laws which criminalise deforestation, nor the scope to introduce them, yet are still affected by extensive and damaging deforestation. Other commentators have highlighted the absence of obligations on investors and financial institutions, who may fund or invest in companies that are involved in deforestation, but who would not themselves ‘use’ those commodities, and would therefore not be obligated by these new supply chain due diligence requirements.

How can lawyers support businesses in building resilient supply chains which are compliant with broader ESG/CSR obligations?

Lawyers have a part to play in assisting businesses build robust, compliant supply chains, which are both fit for purpose and which meet corporate ESG/CSR objectives.

Among other things, lawyers can primarily assist through:

- supporting the implementation of effective due diligence systems to vet new and existing suppliers, including devising and inclusion of pre-contract compliance checks/checklists and questions, supplier mapping (including through the tiers of supply to the suppliers’ supplier and beyond) and risk assessments, etc
- due diligence support which may include detailed information gathering about the commodity/product, where it is produced and details of relevant local regulation, risk assessment and risk mitigation steps, as well as evaluation and continual improvement
- assisting with supplier codes of conduct generally, including those aimed at forest risk commodities, and consideration of appropriate ISO guidelines (eg ISO 14000)
- drafting contractual protections, such as audit rights, preservation of information, records and documents, seeking appropriate supplier warranties, compliance with local laws/industry standards, seeking/ensuring flow down of provisions into sub-

supplier contracts, as well as supplier step in provisions and enforcement rights, etc

- active policing of contracts and best practice in conjunction with the business, including proactive, ongoing two-way engagement with and management of suppliers (eg rewarding good behaviours, enforcement against non-compliance), collection and analysis of supplier return information, etc
- drafting provisions allowing for contractual termination for supplier non-compliance/failure to remediate, including advice to business on risks from termination and mitigation
- advice and support to businesses contemplating engagement with NGOs, competitors and/or other industry players (ie potential collaboration with those facing/tackling similar industry challenges, etc) on environmental compliance
- ongoing monitoring and horizon gazing as to further, future changes to ESG regulation and secondary legislation
- advice in respect of corporate reporting and compliance obligations
- assisting with certification issues
- assisting with reputational issues flowing from supplier non-compliance
- dealing with investor requirements and queries
- handling direct consumer action and supplier litigation
- advice in respect of data protection issues arising from use of AI/data analytics, and
- assistance with insuring for ESG risks

Looking a little further ahead, businesses will likely increasingly look to technology, as some have done already (eg in the food and automotive industries), to deliver solutions to environmental and other supply chain compliance challenges. For example, blockchain will likely assist supply chain due diligence efforts, particularly around tracing, provenance and transparency objectives (ie access to data from field to fork or raw material/commodity through manufacturer to consumer). Lawyers can support companies in this area, including by assisting with acquisition of blockchain companies or putting such blockchain as a service contracts in place with providers.

Consultation

Following the establishment of the enabling framework in the Environment Act 2021, the government has swiftly issued a consultation on the implementation of new due diligence requirements on forest risk commodities. The consultation seeks views on many aspects of the new regime, including which commodities will be considered ‘forest risk commodities’; which businesses will be subject to the new requirements; what they will have to do and what they will have to report in relation to their due diligence; what information will be made public; and how the obligations will be enforced.

Seven commodities are proposed for initial inclusion (cattle (beef and leather), cocoa, coffee, maize, palm oil, rubber, and soy), but with a phased approach, so that the regime would not apply to all seven at first. Additional commodities may also be added subsequently. Business size thresholds will be based on turnover, and the threshold may vary between commodities. The consultation seeks views on a range of turnover threshold options, between £50 and £200 million, as well as addressing other issues such as the treatment of non-UK entities, and exemption tonnage thresholds (under which the requirements will not apply). The consultation also seeks views on the due diligence system to be established, including the use of existing certification schemes and standards. In relation to enforcement, the proposals are for a range of civil sanctions to be available, with a maximum variable monetary penalty of £250,000, in line with other regimes, such as the Ivory Act.

The consultation does not indicate a timeline for the new regime to take effect, but states that the government intends to lay initial secondary legislation at the earliest opportunity. However, businesses would have a period of time to prepare before the beginning of the first reporting period. The consultation is open for responses until 11 March 2022.

Written by Anita Lloyd, Director at Squire Patton Boggs, specializing in environmental and sustainability matters. Simon Garbett, Partner at Squire Patton Boggs, Simon's practice is global in scope and includes both public and private sector clients. Areas of key focus are cross-border disputes, manufacturing, supply chain and product liability issues

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