

Version 3.0

Due Diligence Guidelines



DUE DILIGENCE
TOOLS



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Introduction

These guidelines provide step by step guidance on how to implement a Due Diligence System (DDS), including how to use the system's tools and templates.

The DDS consists of tools that have been developed to support companies worldwide in excluding illegal timber from their supply chains. The system is designed to match all requirements of the EU Timber Regulation, as well as the US Lacey Act and the Australian Illegal Logging Prohibition Act. Though not 100% identical, these legislations significantly overlap in scope and intent.

Note: The following symbols are used throughout this document:



Refers to specific tools that are useful at certain stages of the due diligence process.



Provides guidance to the user and specific relevant information.

Disclaimer: The NEPCon Due Diligence System (DDS) aims to support companies in managing the risk of sourcing, producing and selling forest products that have been illegally harvested, transported or traded. The responsibility for the use of the DDS remains with the person or legal entity using the system. NEPCon waives any liability for the use of the system and shall not assume any responsibility for any loss or damage caused by using the NEPCon DDS.

The NEPCon Due Diligence Guidelines

These guidelines describe a stepwise approach to implementing due diligence that will support conformance to existing market regulations, such as the EU Timber Regulation, the Lacey Act, the Australia Illegal Logging Prohibition Act, etc.

Step 1: Meeting Due Diligence System requirements

Due diligence involves consistent implementation of systems and procedures. Therefore, the NEPCon DDS includes several templates that may be used to ensure that systems and procedures are developed and implemented effectively. The specific templates are referenced for each step below.

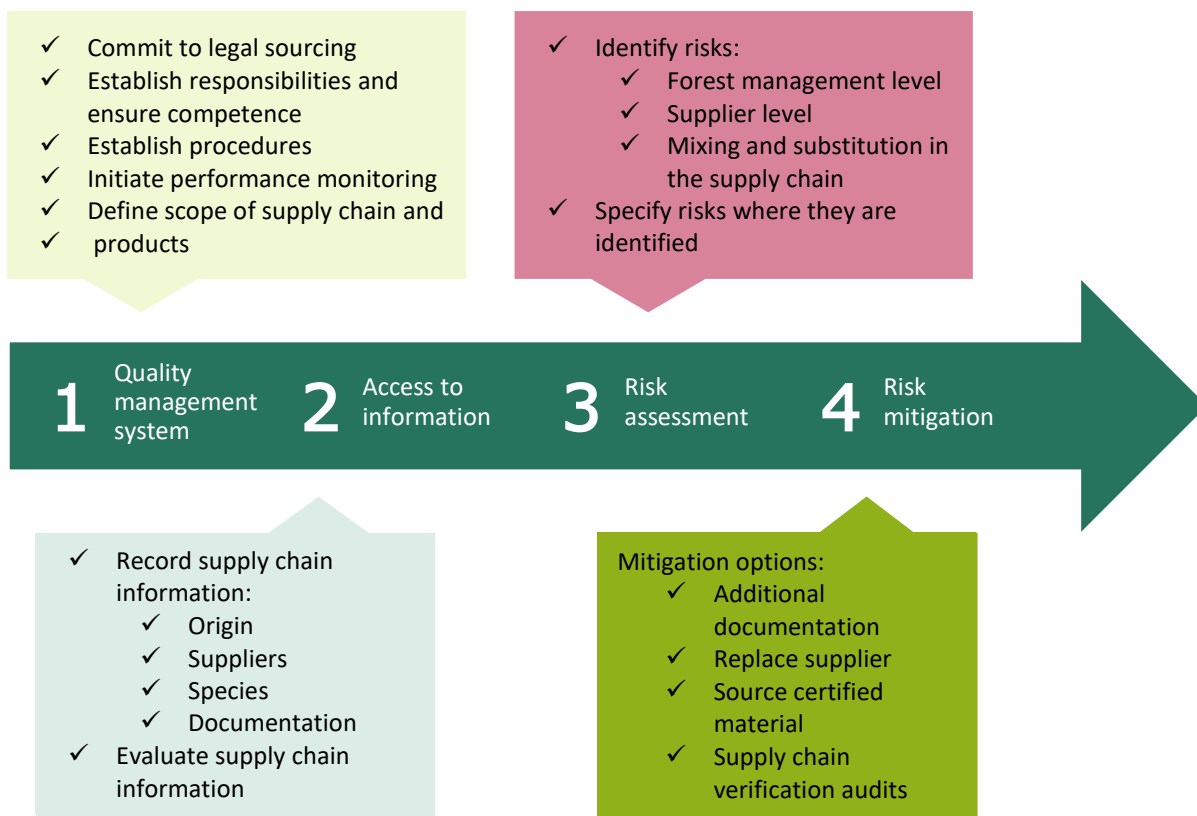


Figure 1: Overview of the stepwise due diligence process

Step 1.1: Commitment to legal sourcing

Establish a policy that forms the basis of your commitment to implementing due diligence. The policy should be signed by senior management.



Use the **Policy Template (DD-03)** and adapt it to your Organisation.



You may reduce the scope of commitment in the template, as long as legality is still included. You may also choose a different format and include different languages. However, the policy still needs to fulfil the basic principles that Organisations shall have a written, publicly available policy, endorsed at executive level, stating an organisational commitment to producing and/or sourcing responsibly by avoiding the production and/or trade of forest products that have been harvested, traded or processed in violation of applicable national legislation and ratified international treaties.

Step 1.2: Define responsibilities and ensure competencies

To ensure proper implementation of your due diligence system, assign responsibility for specified activities to relevant people or positions. Overall responsibility for the DDS is also assigned to one position.

Responsibilities should be assigned to people or positions that have the necessary competencies for the task. Designated people need sufficient authority and access to adequate resources to effectively implement the DDS.



Staff responsibilities and competencies should be documented, as seen in the **Due Diligence Procedure Template (DD-02)**.

Step 1.3: Establish documented procedures

Develop written procedures covering all aspects of the DDS. The procedures should be signed by senior management.



Use the **Due Diligence Procedure Template (DD-02)** as the basis and adapt it to your Organisation.

Step 1.4: Establish quality control and performance monitoring

Establish a system for monitoring compliance with the due diligence requirements. The system should include internal monitoring of:

- The DDS to ensure the system functions effectively, responsibilities are clear, and procedures are implemented; and
- Supply chains to ensure that risk assessments are reviewed annually and whenever supply chains change.

The monitoring system may also include monitoring of suppliers, where an own-verification programme is applied (see Annex 5 for more details).

As part of the quality control system, procedures should be developed to record and address substantiated complaints from stakeholders regarding the DDS and legality risk in supply chains.

Step 1.5: Scope of the due diligence system

Outlining the scope is a central activity of the due diligence process. It is necessary to define and document the suppliers, products, material supply chains, and timber sources that are covered by the due diligence system.

Step 2: Supply chain information and management

A key activity in your DDS is securing access to information about your supply chains and sources of timber products. Information must be available to a level of detail where low risk can be concluded, or to a level where risk mitigation actions can be established. This applies to all products, types of material, and supply chains.



Note that due diligence is significantly more challenging for complex/composite products which include many species or material from different forest origins because information must be collected for all timber sources.

Evaluating the information and documents that can help indicate the legal status of materials and products is an important step in the due diligence process. Information should be evaluated to ensure that complete and correct information is available before the risk assessment can commence.

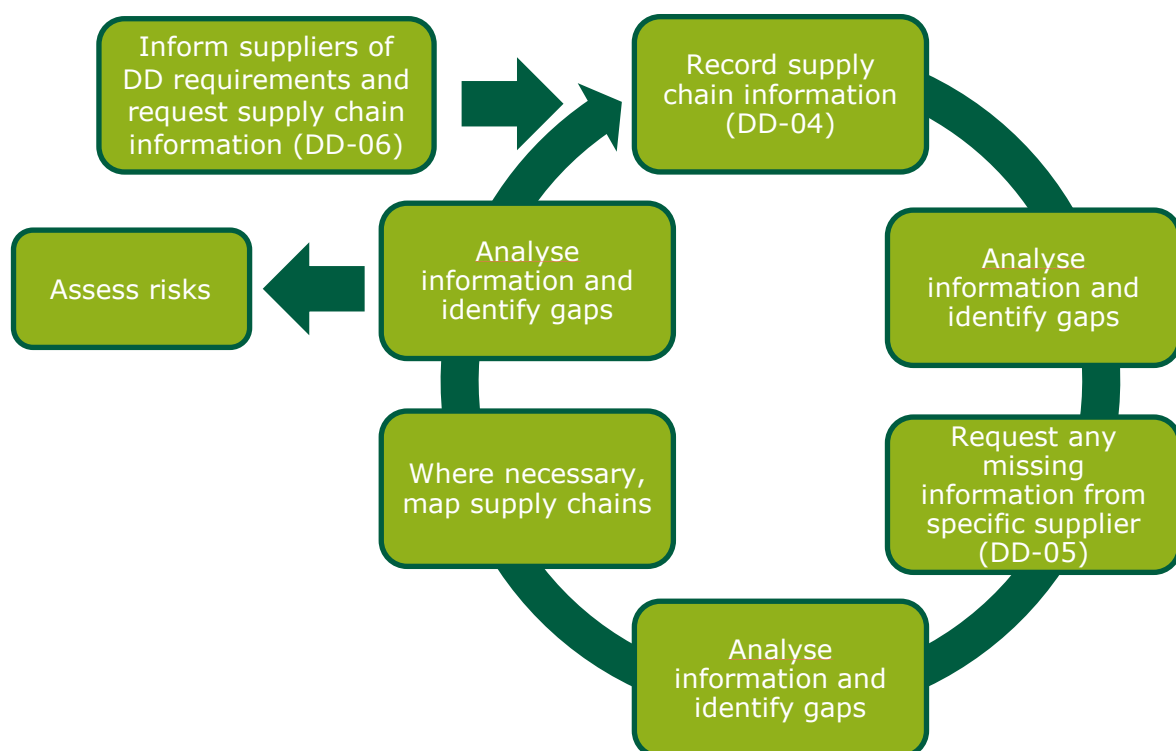


Figure 2: The information collection process

Step 2.1: Collect supply chain information

A prerequisite for an efficient due diligence process is access to a certain level of information. As a general rule, information about the origin of material should be available to a level of detail that allows you to take justified decisions about the origin and the risk of illegal harvest, trade and transport. The following information should be collected and recorded at the onset of the process:

- ✓ the type of product (trade name and type of product);
- ✓ the species of trees shall be clearly identified (by trade name and scientific name);
- ✓ quantity of material purchased and sold (expressed in volume, weight or number of units);
- ✓ the country of origin and, where necessary, the sub-national region of harvest and the concession of harvest;
- ✓ name and address of supplier from which the Organisation has purchased material;
- ✓ name and address of buyers to which the Organisation has supplied products; and
- ✓ the certification/verification status of the material.

To manage your relationships with suppliers and ensure that you gain access to sufficient supply chain information, inform all suppliers of your due diligence activities and request their collaboration. Ensure that you inform suppliers in writing and receive written confirmation that they have understood your due diligence requirements and consent to provide sufficient information.



Adapt and send the **Supplier Letter (DD-06)** to all suppliers at the start of the due diligence process. Receive a signed copy from the Supplier to indicate that they understand and agree to collaborate.



You may wish to include requirements for providing relevant and accurate supply chain information in your commercial contracts with suppliers, instead of/in addition to using the **Supplier Letter (DD-06)**.



Use the **Supplier Information Form (DD-05)** to collect supply chain information directly from Suppliers. This form can be emailed directly to suppliers alongside the Supplier Letter (DD-06). Ask suppliers to complete and return the form or specific sections of it.



Box 1: Collaboration with suppliers

Working with suppliers in all steps of the due diligence implementation is fundamental. A close working relationship with your suppliers facilitates your access to information as well as your ability to assess and mitigate risk.

Communication and collaboration with suppliers and sub-suppliers is a key activity in all steps of your due diligence process.

Step 2.2: Record supplier information

Record relevant information about your supply chains. Where additional information is required about supply chains, contact your supplier and ask them to complete a supplier return.



Use the **Supplier Management Form (DD-04)** to record relevant information about your supply chains based on your existing knowledge. This document may be used as your master document, providing an overview for all your supply chains. For composite products, the form contains a separate tab for recording information about each type of material making up component products.

Step 2.3: Evaluate documents and information

Evaluating information and documents collected from suppliers is a vital part of the due diligence process. If information about a product is lacking, or if information is inadequate to enable effective risk assessments, this constitutes a risk which needs to be mitigated to so that further risk assessment can be conducted.

Box 2: Evaluating Documents

Though documents and records must be collected to enable risk assessment; collection of documents is not a self-standing requirement. Documents without proven relation to the product or that may have been generated illegally have no value in assessing risks. To assess the value of documents some concerns must be evaluated:

- Is the document related to the product?

Often documents are offered as means of indicating legality in supply chains. However, it may be challenging to evaluate how such documents relate to the specific supply chain or material. Often it is not possible to arrive at a firm conclusion about the relationship of documents to supply chains, but there are certain indicators that can be used to evaluate the likelihood that they are not. This may include issues such as dates of issue, location of issuing body, types of licenses (forest types), species identification on documents, volumes, qualities and dimensions of material on documents and conversion factors through processing.

- Can the validity of the document be verified?

The validity of documents is very hard to assess. In many countries with high levels of corruption, it is possible to purchase original documents through corrupt practices to cover up illegal activities in the supply chain. In such cases, it may not be possible to distinguish valid documents from invalid ones. In certain cases, the quality of logos and document layout may be used as an indication of fraud. This has been documented with Chain of Custody and Forest Management certificates.

- Is the document relevant for legality assessment?




The relevance of documents to the supply chain may be evaluated in terms of the role that the document plays in indicating legality. Each document should be evaluated and its relevance to the legality in the specific step of the supply chain identified. NEPCon has published several country profiles which include a list of key documents for different

parts of a supply chain. Some countries also have detailed “Document Guides”, which include copies of example documents and key information they contain.

See **Annex 2** for further risk identification guidelines related to evaluating supply chain documents.

Box 2, above, provides guidance regarding evaluation of supply chain documents provided by suppliers. Table 1 provides a non-exhaustive list of examples of supply chain documentation which may be relevant to assessing timber legality risk.

Table 1: Examples of document evidence related to the five main legality categories

	Legality category	Type of records Generally available documents in paper or electronic format e.g.:
	<ul style="list-style-type: none"> 1. Documentation for rights to harvest timber within legally gazetted boundaries. 	<ul style="list-style-type: none"> • Documentation of ownership/land use rights • Contract or concession agreements • Concession licence • Concession maps • Harvest permits
	<ul style="list-style-type: none"> 2. Payments for harvest rights and timber including duties related to timber harvesting. 	<ul style="list-style-type: none"> • Commercial Contracts • Logging permit • Bank notes • VAT documentation • Official Tax receipts
	<ul style="list-style-type: none"> 3. Timber harvesting, including environmental and forest legislation including forest management and biodiversity conservation, where directly related to timber harvesting. 	<ul style="list-style-type: none"> • Official audit reports • Environmental clearance certificates • Approved harvest plans • Logging permits • Coupe closure reports • Publicly available information demonstrating rigorous legislative supervision and timber tracking and control procedures • Official documents issued by competent authorities in a country of harvest etc.



- **4. Third parties' legal rights** concerning use and tenure that are affected by timber harvesting, as well as worker's rights.

- Environmental impact assessments
- Environmental management plans
- Environmental audit reports
- Social responsibility agreements
- Specific reports on tenure and rights claims and conflicts
- Health and safety records



- **5. Trade and customs**, in so far as the forest sector is concerned.

- Transport permits
- Log removal passes
- Contracts
- Bank notes
- Trade notes
- Import/export licences
- Official receipts for export duties
- Export ban lists
- Export quota awards

Step 2.4: Collect additional supply chain information

After collecting and evaluating information and supporting documentation from suppliers you may have identified gaps in your supply chain information, or concerns about the relevance, accuracy or applicability of information provided. In this step, you will collect additional information to close gaps or address concerns.

If you do not have sufficient information to properly assess the risk, you need to collect further information about your suppliers and/or the origin of the product. For example, there may be lack of information about the country of origin, about the supply chain or about species.



Use the **Supply Chain Mapping Tool (DD-07)** to record details about each supply chain. This may be used where information is needed about up-stream suppliers or the structure/complexity of the supply chain.



Once additional information has been collected, you should update information in the **Supplier Management Form (DD-04)** to attain a complete supplier overview.

Step 3: Risk assessment

The objective of the risk assessment is to identify products or supply chains where risk exists that material entering the supply chain has been illegally harvested, transported or traded. In Step 2, you secured access to information on your supply chains. In Step 3, you shall assess the risk that illegal material is included within those products.

The risk assessment step can be divided into two distinct parts: **Risk Identification** and **Risk Specification** (shown in Figure 3, below). This section introduces identifying and specifying risk, as well as verifying the presence of legal non-compliance in the supply chain.

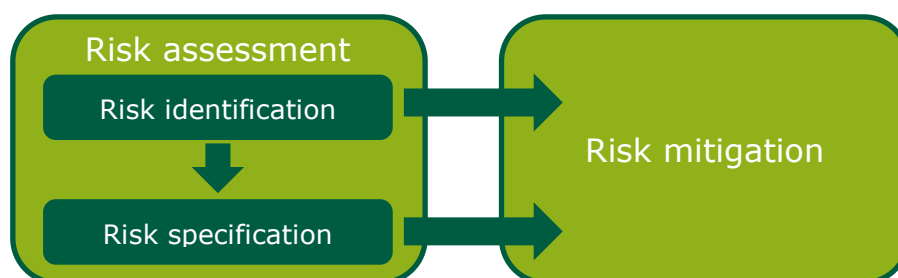


Figure 3: The risk assessment process

Risks can be identified at different levels: country, sub-national or forest. The most efficient process involves *identifying* risk at a national level first, followed by more detailed risk *specification* at sub-national or forest level (where applicable).

The source of risk may vary between different products, supply chains or species. The risk assessment should therefore consider the following:

1. Risk of legal violation in connection with **forest management** and harvesting operations;
2. Risk of legal violation during **trade and transport** of the material throughout the supply chain;
3. Risk that **legally-harvested material is mixed** with other material during processing and trading.



Note that risk assessment is often not carried out in a single linear process, but typically involves iterative steps. For example, if you have collected additional information about a product, you need to re-evaluate the completeness of that information. Newly gathered information may also give rise to renewed processes of risk identification and specification.

Step 3.1: Risk identification

Initial risk identification forms the basis of the risk assessment process, and may often be detailed enough to make justified decisions on how to proceed with managing risks. Risk may be relatively easily identified within several different categories:

- ✓ Access to information
- ✓ Species
- ✓ Origin
- ✓ Certification/ verification status
- ✓ Supply chain complexity
- ✓ Trade and transport



Annex 2 of these guidelines introduces the risk identification process.



DD-08 Risk Identification Checklist Template provides a template to conduct risk identification on specific supply chains. Insert the detailed risk findings in the checklist, remembering to record the sources of information used/ evidence collected, risk assessment process, justification and risk conclusion.



Also, record the risk conclusion in the **Supplier Management Form (DD-04)** to provide an overview of risk across all supply chains.



The conclusion of the risk assessment shall be “Low” or “Specified”

If risk is concluded to be “Low” using **Annex 2 of these guidelines** and **DD-08**, the product can be concluded to have low risk of illegal logging and no further action needs to be taken.

If, on the other hand, the risk cannot be concluded to be low, proceed to the next step in the due diligence process.

Step 3.2: Supply chain mapping

Where risk has been identified, it is suggested to map the supply chain in detail to further evaluate and specify the risks (if not done so already).



The **Supply Chain Mapping Tool (DD-07)** can be used to record supply chain information at a detailed level.

Step 3.3: Specify risk

If you are unable to conclude “low risk” for any product using the steps 3.1 – 3.2, you need to specify the risk to judge if and how the identified risk can be mitigated. Alternatively, jump to step 4 and implement risk mitigation straight away without further specification, if there are obvious options for risk mitigation, for example, by replacing the supplier.



Annex 3 of these guidelines provides guidance on how to specify risks.



Even if a country, region, species or product type has an associated risk of certain legal non-compliances, these may not necessarily be present in your supply chain. Therefore, it is necessary to evaluate risks for each individual supply chain.



Detailed forest legality risk assessments for over 60 countries can be found on NEPCON's website www.nepcon.org. These should be used to identify specific areas of legality risk and ensure suitable mitigation actions are implemented.



Where a national risk assessment is not available, the **Forest Legality Risk Specification Guidelines (DD-09) and Template (DD-10)** may be used to specify risk against the category of law where risk has been identified.

Step 3.4: Verify presence of non-compliances

Before a risk can be mitigated, it should be verified that the potential legal non-compliance is in fact present in the defined supply chain.



The **LegalSource Standard¹ annex 1 and 2** contains tables with verifiers for forest level and supply chain legality risks respectively. Also, the **NEPCon Supplier Audit Report Template (DD-14)** can be used during supplier audits to confirm the level of legal compliance at different levels in the supply chain.

Step 3.5: Record the risk assessment conclusion

Record all conclusions made based on your risk assessment.



Use the **Supplier Management Form (DD-04)** to enter the risk conclusion for each supplier or product.



If the specific product originates from a complex supply chain or is a composite product, remember to conduct risk assessment for each individual supply chain.



The conclusion of the risk assessment shall be “Low” or “Specified”.

¹ The NEPCon LegalSource Standard sets out the LegalSource requirements for producing and sourcing legally harvested timber. It is used for evaluating and certifying due diligence in legal timber sourcing. Download the standard here: www.nepcon.org/legalsource-standard

Box 3: Using Certification as part of the Risk Assessment

Sourcing materials certified according to a third-party legality or sustainability scheme (such as FSC, PEFC, VLC or LegalSource), may be a useful route to reducing risk in your supply chains. However, there is no green lane for certified materials under the EUTR. Risk assessment must still be conducted on these products. The questions are 'why?' and 'how?'

Whilst schemes often cover similar requirements, each certification standard is different. It is therefore necessary to assess whether the certification scheme includes requirements covering the risks relevant to your supply chains. For example, if you have identified that there is risk regarding health and safety during timber harvesting operations in the country of harvest, then you should ensure that the certification standard includes clear requirements for the auditor to check that staff are wearing appropriate personal protective equipment (PPE) during logging operations. If such requirement(s) are not included, then you have no guarantee that this risk has been assessed/mitigated by the certification scheme in question. As a result, you would need to implement additional risk mitigation action to address this risk.

When using certification as part of the risk assessment process, it is important to;

- ✓ Conduct and document your assessment of the certification scheme.
- ✓ Mitigate any gaps or risks relating to the certification scheme.

Where a certification scheme is found to offer sufficient and relevant control of risks identified, you should;

- ✓ Ensure that the materials you are purchasing arrive with valid certification claims/ information (e.g. the certification claim and code is displayed on the supplier invoice and delivery note).
- ✓ Ensure the certification claims/ information are valid and accurate (e.g. by checking the certification scheme online database or contacting the auditing body).



The **Certification System Evaluation Checklist (DD-13)** can be used to record the certification scheme assessment.



The **NEPCon Certification Scheme Evaluation Standard (LS-18)** contains the formal requirements for certification system evaluation.

Step 4: Risk mitigation

If risk is concluded to be present in the supply chain, the risk must be mitigated. Risk mitigation measures must be implemented for all products or supply chains that are classified as 'specified risk'. Mitigation must occur before the product is purchased/sold.

Step 4.1: Identify risk mitigation actions

Once it has been verified that the underlying non-compliances giving rise to risks do exist in the supply chain, the next step is to identify suitable risk mitigation actions. Identify and select actions that are effective in addressing the specified risk.

The appropriate mitigating measures depend on the type of potential legal non-compliance in question. Some types of non-compliances can be verified by field visits to the harvesting sites (e.g. inspecting the borders of the harvesting unit, workers' use of personal health and safety equipment, level of soil damage). Others can be verified based on document control (such as custom declarations forms, payment of royalties, work permits etc.). In some cases, a combination of different control measures may be required in order to ensure proper risk mitigation.

There are two broad groups of mitigation action that may be employed: **risk avoidance** and **risk control** (see Figure 4). It is impossible to discuss all risk mitigation actions and alternatives not mentioned in this guide should be considered, if applicable to mitigating risk in your supply chains.



Annex 4 of these guidelines provides more detail on risk mitigation actions.

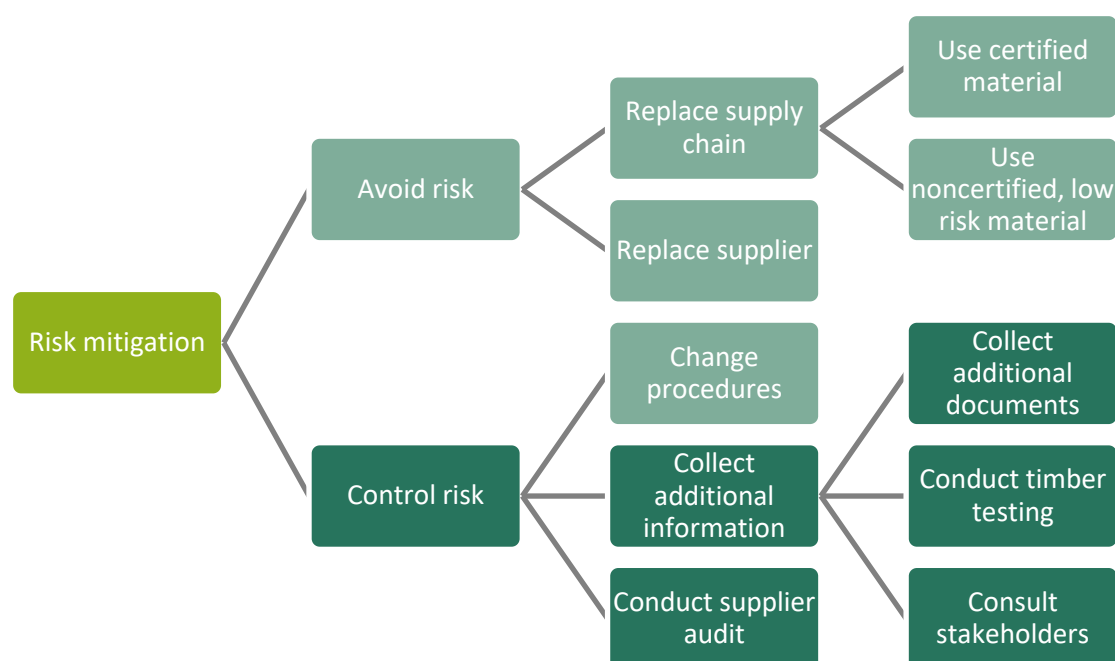


Figure 4: Risk mitigation options

In almost all cases risk mitigation will require the collaboration of one or more of your suppliers. Working with them is therefore necessary to mitigate risks.



In cases where it is not viable or possible to work with sources or suppliers to actively mitigate specified risks, the only options are to stop sourcing that product or change to a supplier/supply chain that can be confirmed to be low risk.

Step 4.2: Obtain consent from suppliers

For suppliers that supply material or products which cannot be confirmed to be low risk the supplier or sub-supplier shall provide written consent to support your organisation in implementing necessary risk mitigating actions.



Where risks are specified at upstream entities of the supply chain, such as the forest, primary processing facilities etc., these should also provide consent to conform to the requirements. Your supplier will play an important role in communicating and obtaining consent from sub-suppliers.



Adapt the **Supplier Letter Template (DD-06)** for sending to your sub-suppliers to secure their consent to support risk mitigating activities and allow auditors to visit their facilities if needed.

Step 4.3: Plan and record risk mitigation actions

Record all planned mitigating actions to keep track of risks and their current mitigation status.



Use the **Supplier Management Form (DD-04)** to plan and track the status of risk mitigation actions.

Box 4: Choosing the right measure

The risk mitigation process depends on the risks specified during the risk assessment. You need to address all the risk aspects: risk of illegal harvesting at the forest level, risk of illegal activities within supply chain entities or risk that material is mixed with illegal material in the supply chain.

Note that different mitigation actions have different merits depending on the type of risk specified. Some risk mitigation actions will not effectively mitigate the risks specified, whilst the same action may be useful in mitigating other types of risk.

For example, conducting an on-site audit of your supplier's manufacturing facility may provide extra confidence that unknown timber sources are not being mixed with known and legal timber sources if it is observed that the supplier has a robust chain of custody system in place. However, this mitigation action would not help mitigate the risk that timber was harvested using child labour at the forest level. To mitigate that risk, a more appropriate mitigation action would be audits at the forest management unit.

Step 4.4: Implement risk mitigation actions

Once you have planned the mitigating actions, manage and oversee their execution.



Use the **Supplier Management Form (DD-04)** to track timely execution of planned actions.



Annex 4 of these guidelines provides guidance on risk mitigation options.

Conducting an audit of organisations within the supply chain may be necessary to mitigate risk. This may require auditing suppliers at the forest-level (forest management organisation) or auditing suppliers within the supply chain (sawmills, traders, factories).



Annex 5 of these guidelines provides guidance on conducting Supplier Audits as part of your due diligence system.





Adapt and use **DD-14 Supplier Audit Report Template** to record supplier evaluation findings.

Step 4.5: Evaluate the effectiveness of risk mitigating actions

Once risk mitigation actions have been implemented, evaluate their effectiveness on a regular basis. It is integral to verify that the mitigation actions that you have implemented have been effective in mitigating the identified risk. Verification should be conducted on a regular basis, to ensure that the risk does not recur in the future.

Table 2: Examples of risks, mitigating and verification actions

	Specified Risk	Mitigation Requirements	Mitigation and Verification actions
	Risk of violations of customary rights at the forest level.	Verify presence of issue at origin – manage legal non-compliance by ensuring management practices includes respect for customary rights.	On-site audit, stakeholder consultations, interviews, document review.
	Risk of violations of customs regulations.	Verify presence of issue at origin – revise procedures where necessary to meet customs requirements.	Verification of custom documents and transport documents from supplier. Consultation with customs authorities.



Risks of violations of harvest regulations related to environmental regulations.

Evaluate presence of issue at origin – Forest Management Unit, forest manager or contractor to change harvest practices to meet requirements.

Forest level verification audits focusing on environmental compliance in forest operations.



Risk of known and unknown materials being mixed in the supply chain.

Work with supplier factory to change segregation procedures for input material and implement chain of custody procedures to eliminate mixing.

Audit of Supplier factory following implementation of chain of custody system. Timber testing to verify absence of mixing of timber from different origins.

Annex 1: NEPCon DDS Tools

The tools listed below are all available in the NEPCon Due Diligence System which is free to download from the NEPCon website (www.nepcon.org).

Code	Name	Description
DD-01	Due Diligence Guidelines	This document. Additionally: Annex 2 Risk Identification Guidelines introduces the risk identification process; Annex 3 Risk Specification Guidelines introduces the risk specification process; Annex 4 Risk Mitigation Guidelines includes a description of the risk mitigation options for different types of specified risks; and Annex 5 Supplier Audit Guidelines provides guidance on verifying supplier's conformance to NEPCon requirements.
DD-02	NEPCon Due Diligence Procedure Template	A template that you can use as basis for your due diligence procedure. It needs to be adapted to reflect your systems and realities.
DD-03	Responsible Sourcing Policy Template	A sample responsible sourcing policy that covers legality and environmental and social responsibility.
DD-04	Supplier Management Form	This form supports you to collect and evaluate supplier information. It facilitates entry of relevant information about suppliers, sources and products as well as related risks identified using the risk identification checklist (DD-08).
DD-05	Supplier Information Form	This form is to be used with DD-06 to collect information about your suppliers and the products/material they supply to your organisation. Your suppliers need to fill in this form with as much information as possible.
DD-06	Supplier Letter Template	Letter template to be used to ask for additional information from suppliers and their consent to undergo monitoring by you or an appointed auditing body.
DD-07	Supply Chain Mapping Tool	Use this form to collect and manage information about sub-suppliers and sources of specific suppliers. Useful in cases where you need additional supply chain detail from your suppliers.
DD-08	Risk Identification Checklist Template	Template to record risk identification results for specific supply chains.
DD-09	Forest Legality Risk Specification Guidelines	Detailed guide to conducting the risk specification process.
DD-10	Forest Legality Risk Specification Template	Excel template used in the process of specifying risks.

Code	Name	Description
DD-11	Due Diligence Guidelines for FMEs	Due Diligence guidelines (the equivalent of this document) for Forest Management Enterprises (FMEs).
DD-12	Due Diligence Procedure Template for FMEs	A template that can be used as the basis of a due diligence procedure for Forest Management Enterprises (FMEs).
DD-13	Certification Scheme Evaluation Checklist	Template for evaluating the scope and coverage of certification schemes according to their ability to provide assurance of legal timber sourcing.
DD-14	Supplier Audit Report Template	Report template to be used by the organisation conducting supplier verification audits.
DD-15	Product statement	Template for suppliers to provide important information about products they are supplying.

Annex 2: Risk Identification Guidelines

The annex below guides you through the risk identification process.



DD-08 Risk Identification Checklist provides a template to collect and record risk identification results.

The NEPCon Risk Identification Checklist (DD-08) is a tool which may be used by Organisations to identify risk in timber and paper supply chains. The checklist categorises risk into five broad categories relating to product and/or supply chain characteristics:

- ✓ Access to information
- ✓ Species
- ✓ Origin
- ✓ Certification/ verification status
- ✓ Supply chain complexity
- ✓ Trade and transport

Using the Risk Identification Checklist

The checklist is designed to be used in the early stages of risk assessment, to provide a broad overview of risk in supply chains. To start an evaluation, simply start at category one and evaluate the risks based on each of the risk identification categories and risk sub-categories. The guidance notes should be used to inform the decision-making process. Supporting links to relevant information are also provided.

For each risk sub-category, the user should evaluate the level of risk for each product or supply chain (where multiple timber sources are used) and describe the risk and cite the evidence used. The last column may be used to provide an overview of whether risk is identified ('specified risk') for the product/ supply chain or whether risk is deemed to be low ('low risk').

Risk assessment is a process that requires the user to make an informed decision about risks. The table cannot provide a decision for all cases and the user is advised to use best judgment and apply a precautionary approach when assessing risks. Additional information may be required to be collected from experts or additional sources. It is good practice to cite the evidence used to reach the risk conclusion and keep records of all documentation alongside the risk identification checklist.

Where risk is identified against any risk sub-category, risk specification shall be undertaken to more accurately assess the extent and severity of risk in the supply chain. See NEPCon Forest Legality Risk Specification Guidelines (DD-09).

Whilst risk may be present against a sub-category, this same risk may have been proactively controlled by the presence of other controlling factors. For example, risk of corruption in supply chains may be negated by the fact that supply chains are certified to a credible certification standard. In these cases, risk should be faithfully recorded against

each sub-category in the checklist. At the end of the checklist relevant mitigating factors may shall be cited for each 'specified' risk sub-category (where applicable).

Where risk is identified against any risk sub-category which is not proactively controlled, the risk shall be mitigated prior to placing timber and paper products on the market.

The following explains the risk identification categories:

Conclusive risk categories

A few factors provide clear and conclusive risk status regardless of species or origin of the material:

- Material supplied as CITES or FLEGT licensed wood is exempt from the due diligence requirements and the risk can be classified as low. It should be underlined that the authenticity of documents shall be evaluated. Cases have been known where CITES licences have not been sufficient to ensure legality, and care therefore should be taken.
- Conversely, timber originating from countries with active UN or EU trade sanctions including timber and/or timber products shall never be sourced and must be excluded from the supply chain. The only way to mitigate this risk is to stop sourcing from these countries².

Access to information

Information on the supply of timber and timber products is crucial in risk assessment. Lacking, incomplete or false information constitutes a risk that requires mitigation before the risk evaluation can be completed. It is necessary to evaluate if the information about a product or material is sufficient and of a quality that enables conclusions to be made about the risk (or absence of risk) attached to the particular product or supply chain.

Species

Certain timber species have been more often connected with illegal harvesting than others. Such species may indicate risk. However, it should be underlined that the species alone may not allow a conclusion about the risk status and that the risk originating from the area of harvesting should also be considered. Therefore, the origin risk must always be considered.

Origin risk

The risk of timber being harvested or traded contrary to legislation applicable in the country of harvest is a key risk criterion. A few sources of information are however available to guide the process of determining risk of illegal activities in a country. In principle, the evaluation of risk of illegal harvesting in a certain country must take into consideration applicable legislation as has been defined by Annex 1 of the NEPCo **LegalSource Standard** as legislation in force in the country of harvest covering the following matters:

² At the date of publishing no countries fall under this category.

- 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.

Detailed forest legality risk assessments for over 60 countries can be found on NEPCon's website www.nepcon.org. For any countries not currently covered, there are a number of sources of information that can support a risk assessment.

The Global Forestry Registry (GFR) is a free source of information on the risk of sourcing controversial timber throughout the world. The registry covers more than 150 countries worldwide. However, for many countries, the information is still limited. Countries listed as "unspecified risk" in the Global Forest Registry for the Category 1 (Legality) are countries where there is higher perception of risk of illegal harvesting.

www.globalforestryregistry.org

The Corruption Perception Index (CPI) may provide a first indication of the risk, and special attention should be placed on countries with a CPI below 50. However, it must be underlined that risk of illegal activities may also occur in countries with a CPI index above 50. This scale does not provide a definite measure of risk: it is only an indicator.

www.transparency.org

Certification/verification status

Certification or verification against recognised standards can play an important role in risk assessment and mitigation. To ensure that third party certification schemes meet the EU timber regulation, NEPCon has adopted requirements to evaluate and recognise systems³. It should be noted that even if material is sourced with a certification claim, the Operator shall still ensure that claims are valid, that the material in question is covered by the certification scope, and that other relevant requirements of the certification system have been met.

Supply chain complexity

Risks originating in the supply chain include the risk that the material received does not correspond to the information accompanying the shipments, meaning that the product has been contaminated with material with illegal origin.

This risk mainly arises when the organisation purchases the same type of material as entities in its supply chain that purchase from different sources or origins that may be illegal.

³ See the document "LS-18 NEPCon Certification Scheme Evaluation Procedure V1" for guidance on how to evaluate certification schemes.

In essence, this relates to the risk of legal material being mixed with material with unknown or illegal origin. The types of material being handled and the risk of mixing shall be evaluated for each entity in the supply chain.

Trade and transport

Even if material is from legally harvested forests, there may be illegal activities occurring in the supply chain that relate to the handling, trade and transport of the material. Annex 2 of this standard contains the definition of issues that need to be considered when evaluating the legality of processing and transport entities included in the scope of a robust due diligence system.

Annex 3: Risk Specification Guidelines

This annex defines the process of specifying risks, where initial risk identification has concluded that risk is present and available information on these risks provides insufficient detail to allow effective risk mitigation.

When risks are identified, it is necessary to specify the risk for each supply chain to enable effective risk mitigation.



Note that the process of specifying national or sub-national levels risks is a complex process that requires thorough research and local capacity. It may not be possible for many organisations to engage in such a process themselves. Detailed forest legality risk assessments for over 60 countries can be found on NEPCon's website www.nepcon.org.

Supply chain mapping

Supply chain mapping is a prerequisite to effective risk specification. In order to specify all relevant risks at the appropriate level, it is necessary to have sufficiently detailed information about all entities of the supply chain.



DD-07 Supply Chain Mapping Tool provides a template to collect and record supply chain information.

Once the supply chain has been mapped to the appropriate level, the risk specification can take place.

Risk specification process

1. Baseline assessment

Initially the **scope and spatial/functional scale** related to the country/region shall be defined – this could mean subdividing the assessment into specific areas or regions (or countries). These are then used to **identify possible additional 'Criteria and sub criteria'** that need to be met to satisfy the Category and each new 'Criteria and sub criteria' shall be accompanied by guidance text.

2. Research

Review the newly identified criteria/sub criteria plus the five generic Criteria and sub criteria, and identify the following for each sub category, while using the applicable spatial scale throughout:

- a. Applicable laws and regulations;
- b. Legal authority;
- c. Legally required documents or records; and
- d. Sources of information.

3. Risk description

- a. Describe the possible risks that can be associated with the category and associated specific criteria and sub criteria.

- b. Evaluate the level of risk that non-conformance is present, considering:
 - i. Threshold for compliance, considering the extent, scale and time frame;
 - ii. Corruption level;
 - iii. Governmental issues; and
 - iv. Available information.
- c. Justify the risks evaluated to be present, referring to the above (threshold, corruption, description etc.).

4. Risk specification

Specify each criteria and sub criteria as either 'specified risk' or 'low risk', based on the evaluation.

5. Establishment of control measures and verifiers

- a. Identify applicable control measure/verifiers in the list of generic control measures/verifiers.
- b. Identify further control measure/verifiers for each criterion and sub criterion. The established verifiers and control measures shall be used to:
 - 1) Verify the presence or absence of non-compliance where risks are specified; and
 - 2) Mitigate risks where the underlying non-compliance is confirmed to be present in specific supply chains.



DD-09 Forest Legality Risk Specification Guidelines contains a detailed description of the risk specification process.



DD-10 Forest Legality Risk Specification Template contains an Excel template for the risk specification details.

Annex 4: Risk Mitigation Guidelines

The purpose of this section is to describe potential risk mitigating actions in case risks of legal non-compliance have been specified in the sourcing area. This annex covers STEP 4 of the due diligence process set out in this guide.

There are two broad groups of mitigation action that may be employed: **risk avoidance** and **risk control** (see Figure 5).

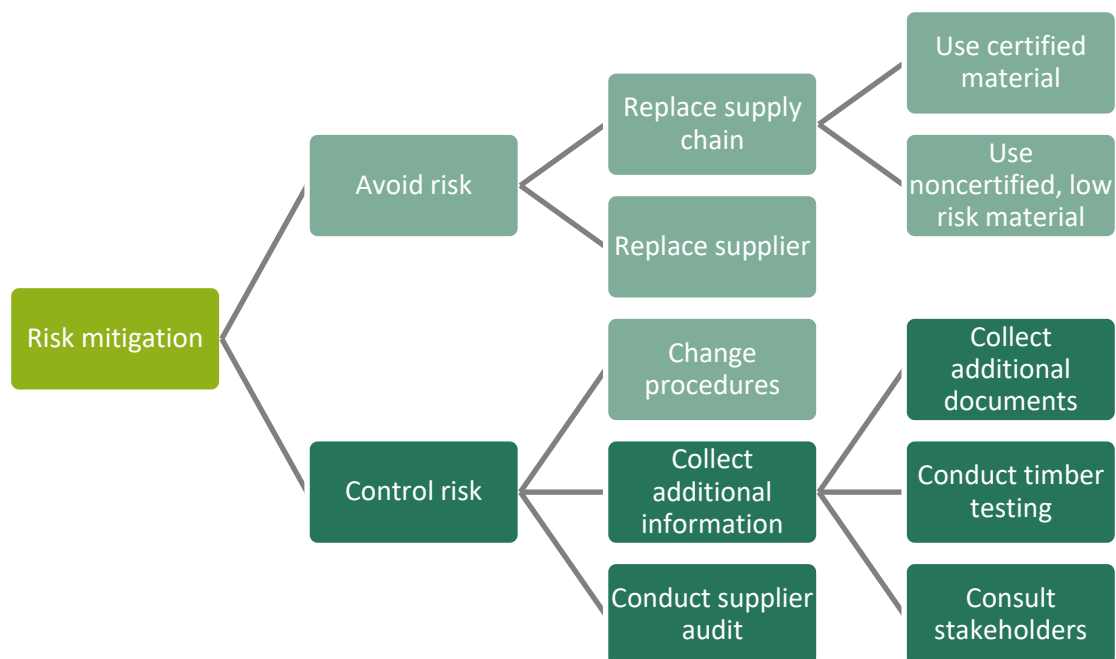


Figure 5: Risk mitigation options

Risk control

Controlling risk may be possible in many supply chains by working with direct or sub-suppliers. The potential methods for controlling risk are:

- **Collect additional information**
 - **Documents:** This may involve collecting additional information which supports a conclusion of low risk. For example, if inconsistencies are detected on documents, additional documents may be collected and cross-referenced to show that the balance of evidence supports a low risk conclusion.
 - **Timber testing:** Additional information may be gathered by sending timber or paper products for laboratory testing. Microscopic fibre testing, DNA analysis and Stable isotope testing can all help to verify species and/or origin of wood-based products. These techniques may be used to verify supplier claims or integrity of documentation where the risk of fraud is present.
 - **Stakeholder consultation:** Where publicly available resources have been exhausted, it may be necessary to consult specific stakeholders directly. This may include, but is not limited to; government authorities, (document) issuing

authorities, advocacy organisations, independent experts (in forestry, law, economics), certification bodies, local communities, etc.

- **Change Procedures:** Implementing additional procedures or changing existing operating procedures may help to mitigate risk. This may be a challenging risk control measure to implement unless suppliers are fully committed to supporting your due diligence process. Changing procedures may involve the supplier implementing a chain of custody system, to provide confidence that inputs to your products are not mixed with unknown and potentially high risk inputs in the factory. It may also involve the supplier implementing a robust record-keeping system, so that supply chain documents are requested and stored for every shipment that you purchase.
- **Conduct Supplier Audits.** Supplier audits may be conducted at the origin to verify non-compliance in forest-level legality requirements, e.g. harvesting within legally gazette boundaries. Or they may be conducted at any point in the supply chain, e.g. at a sawmill, furniture factory, paper mill, trading office, etc. Supply chain audits typically focus on ensuring legal trade and chain of custody.
 - **Second-party audits:** Second-party audits are those conducted by a member of your Organisation, upon your supplier.
 - **Third-party audits:** Third-party audits are those conducted by an independent Organisation on your behalf. Organisations often prefer to employ an expert third-party which specialises in conducting supplier audits, to add credibility to the verification process.

See **Annex 5** for detailed supplier evaluation guidelines.

Risk avoidance

Risk avoidance measures aim to bypass or exclude the identified risk from the supply chain. This may include:

- **Changing Supply Chains.** Making changes to supply chains may be done in collaboration with suppliers to avoid the risk associated with particular species, materials or origins. For example, where there is clear evidence that a species is often illegally harvested in the country of origin, suppliers may be able to provide the same species from lower risk countries, where illegal harvesting is not a risk.

Alternatively, using supply chains certified to an independent third-party certification scheme may offer robust mitigation. When considering whether to use certified materials, you should consider the scope and integrity of the certification scheme in question, to ensure that the scheme covers the specific risk identified in your supply chain(s).
- **Replacing suppliers.** Where a supplier is unwilling or unable to work with you to implement other mitigation actions, the only option may be to end the relationship with that supplier. Often direct suppliers are willing to engage in the risk mitigation process, but sub-suppliers are not. In these cases, it may be necessary to agree with the direct supplier that only certain complaint sub-suppliers shall be used for your products.

Risk mitigation activity	Explanation	Examples of usage
Supplier collaboration/ Change Procedures	Close collaboration with suppliers is a fundamental issue of managing supply chain risks. Therefore, communicating clearly and working closely with suppliers will be a key activity in almost any risk mitigating activity.	Combination of identifying the risk, agreeing risk mitigation action with supplier (legally binding), ensuring supplier is competent to implement the actions, and verifying that the actions are taken and effective.
Stakeholder consultation	Consultation with stakeholders can be done in several ways depending on the type and location of the group or entities to be consulted. Where large groups need to be consulted, meetings or workshops can be arranged to gather inputs and information. If the consultation involves few individuals or single entities, interviews may be conducted either face to face or via phone or email.	Evaluation of potential violations of third parties' rights in connection to forest management activities may include consultation with groups or entities that potentially hold rights to the area in question. It should be stressed that the type(s) of stakeholders relevant for different types of evaluations differs. In some cases, stakeholders will be limited to e.g. government officials, while in other cases relevant groups may include indigenous people's representatives, NGOs and/or local communities.
Document verification	Document evaluation is relevant only where the documents can be connected to the material or product in question. Document control involves evaluating the validity and correctness of documents related to the origin and legality of forest management activities, trade, or processing, and may involve a host of different types of documents and records. This may also include getting missing documentation that is critical for either supply chain information or proving certain aspects of legality.	Document verification can be used to verify the existence of valid harvest permits for a defined forest area.
Field audits/ verification	Where risk has been specified that cannot be evaluated by document review, on-site audits of specific	If the specified risk concerns e.g. harvest practices, on-site observation of actual harvesting is required in order to evaluate

Risk mitigation activity	Explanation	Examples of usage
	<p>areas or entities may be needed to confirm that the activities undertaken are legal. On-site verification is only effective when the risk relates to activities that require observation on the ground. However, it must be stressed that field verification is a key tool to evaluate the effectiveness of risk mitigating actions.</p>	<p>the relevance of the specified risk at the particular site. This could involve evaluation of the use of safety equipment during harvest, or the application of specific harvest methods required by law.</p>
Third party verification	<p>Third party verification can be used when the organisation engaging in NEPCon certification does not opt to implement its own verification system. In this case a third party can be contracted to carry out the necessary evaluations on the organisation's behalf.</p>	<p>Third party verification can be applied for all types of verification audits, at processing level and forest level. An example may be an evaluation of a processing facility's ability to separate materials carrying different claims through the processing. This lets the organisation verify that they do not risk sourcing material with unknown or illegal origin that has been mixed into their products during processing.</p>

Table 5: Examples of risk mitigating measures

Annex 5: Supplier Audit Guidelines

Supplier verification audits may be needed to establish whether a risk of legal non-compliance is present at the source/supplier. Verification can also be used if risk mitigation actions have been effective in controlling or managing the underlying cause of the non-compliance.

The below provides guidelines to companies that wish to implement their own verification programme.

Verification therefore plays an important role in the whole due diligence process.



Companies that do not wish to implement their own verification programme may employ a 3rd party auditor organisation.



The **Supplier Audit Report Template (DD-14)** supports you in conducting supplier verification audits and record findings in a systematic way.



The **LegalSource Standard Annexes 1 and 2** contains tables with verifiers for forest level and supply chain legality risks respectively. Whilst the **NEPCon Generic Chain of Custody Standard** includes requirements for reducing the risk of mixing in supply chains.

Supply chain verification audits may cover Forest Management Enterprises, traders or processing facilities, or both.

Supplier verification requirements differ significantly between these two main types of audits. These differences are clarified below.

Verification objectives

Supplier/source verification may have two objectives:

1. Verify the absence or presence of potential legal non-compliances based on the specific risks identified during the risk assessment.
2. Verify if due diligence system and/or agreed risk mitigation measures have been implemented effectively and that the risk has been mitigated.

One verification process may include both the above in one process.

Audit scope

You must determine the scope of the verification prior to designating an auditor and scheduling the audit.

The scope of the verification audit must correspond to the specified risks or the specific responsibilities of your supplier. This means that the audit may only relate to some risks or activities and not to others. This is important in terms of establishing the audit requirements and needed auditor competences.

The scope definition of the audit includes determination of:

- Type of entities included in the audit (single processing facility, multiple processing facilities, single Forest Management Unit/FMU, multiple FMU);
- Identification of specified risks that will be evaluated; and
- Site visits required in the audit evaluation. Site visits depend on the location and number of FMUs included in the scope of the evaluation and the audit team composition.

The supplier's role in the verification process

Suppliers play a key role in most verification processes. Suppliers are normally closer to the forest of origin, where risks may often be found, and may thus be in a good position to help identify and mitigate risks.

The role of your supplier is not necessarily limited to providing access to information. On the contrary, suppliers can play a key role by becoming directly involved in the verification process. In some cases, this may require training; however, in the long run, using local capacity is often more effective and efficient.

Naturally it is important that the supplier's role has been clearly defined and agreed beforehand. All involved need to be aware of their roles and responsibilities and have the necessary competence and authority to enable the process.

Audit preparation

In any case the preparation for audits needs to be well planned and communicated between the organisation implementing them and those being audited.

Your supplier is expected to prepare for a verification audit by providing information required for the evaluation of the specified risk areas. Depending on these risks and on the role of your suppliers in the due diligence system implementation, they should provide the following prior to the evaluation:

- Confirmation of their acceptance of the verification audit;
- Documented procedures;
- Records and systems that document the actions taken to mitigate risks;
- Identification of responsible staff;
- Defined scope of the material;
- List of supply chains and all sub-suppliers included in the scope;
- Risk assessment records (if applicable);
- Legality documentation for material included in the scope (if at the forest level this could include forest management plan, licenses, etc.); and
- Records showing compliance with relevant laws and regulations of the entity themselves.

Evaluation of processing and trade entities

Verification of suppliers that are classified as processing or trade facilities may be carried out on-site or by desk evaluation depending on the risks that have been specified. Onsite verification may include interview with relevant staff, review of documents (procedures and records of processing) as well as observation of practices in processing.



Verification requirements: The requirements for suppliers included in a verification program are found in ***Annex 2 of the LS-02 LegalSource standard.***

Evaluation of forest management enterprises (FMEs)

The verification of forest sources of timber addresses any specified risks identified to be present in a country, sub-national region, FME or group of FMEs.



The requirements for verifying FMEs are found in ***Annex 1 of the LegalSource standard.***

During the evaluation, confirm that the FME conforms to all relevant legality issues that have been defined as specified risk during the risk assessment. A legality category that has been confirmed to be low risk does not need to be evaluated.

Auditor competence

The reliability of the audit process depends on the competencies of those conducting the audit. The auditor's competence consists of the personal and underlying attributes deriving from their education, previous work experience, auditor training and auditing experience.

Finally, it is important for any auditor to have a thorough knowledge of the system and the standard to which they are auditing. Knowledge of legal requirements and the legal context is also very important.

The competence of auditors covers the following aspects:

- a) *Audit principles, procedures and techniques:* the auditor must be able to apply those appropriate to different audits and ensure that audits are conducted in a consistent and systematic manner.
- b) *Management system and reference documents:* the auditor must comprehend the scope of the audit and the applicable audit requirements.
- c) *Organisational context:* the auditor must understand the organisation's operational context. Knowledge and skills in this area should cover:
 - organisational size, structure, authority, functions and relationships;
 - general business processes and related terminology; and
 - cultural and social customs of the auditee.
- d) *Applicable laws, regulations and other requirements relevant to the discipline:* the auditor must be able to work within, and be aware of, the requirements that

apply to the organisation being audited. Knowledge and skills in this area should cover:

- local, regional and national codes, laws and regulations;
- contracts and agreements;
- international treaties and conventions; and
- other requirements to which the organisation subscribes.

Conformance evaluation

The suppliers that are included in the verification audits under an organisation's due diligence system needs to be able to provide evidence that they are in conformance with the relevant legality requirements. As mentioned above, the specific requirements applicable depend on the risks that have been specified, as well as the type of entity under evaluation. The NEPCon standard contains required verifiers that need to be evaluated for each specific type of legality requirement.

It is important that conformance with the standard requirements are evaluated and documented. Any non-conformances against the requirements should be defined and specific corrective action requests should be raised and given a defined timeline.

Reporting

The results of verification of suppliers shall be documented in a systematic and transparent way.



The ***Supplier Audit Report Template (DD-14)*** contains the relevant checklists for all types of audits and may be used.

About

Supporting Legal Timber Trade

Supporting Legal Timber Trade is a joint project run by NEPCon with the aim of supporting timber-related companies in Europe with knowledge, tools and training in the requirements of the EU Timber Regulation. Knowing your timber's origin is not only good for the forests, but good for business. The joint project is funded by the EU LIFE programme and UK aid from the UK government.



About

Responsible Sourcing of Soy, Cattle and Palm Oil

Responsible Sourcing of Soy, Cattle and Palm Oil is a project aimed at creating awareness and capacity among Danish companies to minimise risks of social and environmental problems connected to sourcing palm oil, soy and cattle from developing countries. The project is run by NEPCon and funded by DANIDA, Ministry of Foreign Affairs of Denmark.



NEPCon (Nature Economy and People Connected) is an international, non-profit organisation that builds commitment and capacity for mainstreaming sustainability. Together with our partners, we foster solutions for safeguarding our natural resources and protecting our climate.

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