
The Announcement of Criminal Charges against Lumber Liquidators Underscores the Need for Lacey Act Compliance

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On Wednesday, April 29, 2015, Lumber Liquidators announced in its most recent 10Q that the United States Department of Justice plans to pursue criminal charges surrounding allegations the company illegally imported wood in violation of the Lacey Act, 16 USC § 3371 et seq. On the heels of this announcement, some leadership re-organization and disappointing earnings, Lumber Liquidator shares were trading as much as 20% lower.

The development with Lumber Liquidators demonstrates that, since its unsuccessful attempts to prosecute Gibson Guitar, the federal government has not lost interest in enforcing the 2008 amendments to the Lacey Act that expanded the scope of the Act to plant products (including products made from wood). As discussed in more detail below, the Lacey Act prohibitions applicable to foreign wood sourcing are quite broad, and require a company to exercise due care in its supply chain, even if it is not the importer of record.

In addition, unlike past high-profile Lacey Act investigations that focused on exotic and potentially threatened species (as was the case with the Gibson investigation), the focus for Lumber Liquidators has been on common hardwoods used in everyday flooring materials. Accordingly, the belief that a company may be insulated from Lacey Act issues because they only deal with abundant wood species appears unfounded.

The cost of being subject to a Lacey Act investigation or enforcement action greatly outstrips the cost of compliance. Companies that are the subject of Lacey Act investigations and enforcement proceedings may face substantial civil or criminal penalties, seizure of goods, disruption of supply chains, negative PR, significant legal fees, and a decline in stock prices. This latter point is proven by the drop in Lumber Liquidators stock prices.

By contrast, robust compliance provides a level of risk certainty in the sourcing of wood products and can be cited as an affirmative example of responsible environmental stewardship. Voluntary compliance will

not only have a positive public relations impact; it has the potential to push particular industries (including competitors) toward the laudable goal of responsible sourcing activities.

Lacey Act Background

The Lacey Act is the oldest wildlife protection statute in the United States. Initially enacted to protect animal species, the Lacey Act was amended, effective May 22, 2008, to include plant species. A major rationale for the inclusion of plant species in the Lacey Act was to prevent trade in illegally harvested lumber, as well as wood products made from such lumber.

The Lacey Act makes it unlawful to:

- Trade in any plant or wildlife product that is taken, possessed, transported, or sold in violation of the laws of the United States, a State, Indian Tribe, or any foreign law that protects plants;
- Falsify or submit falsified documents, accounts or records of any plant covered by the Lacey Act; and
- Import plants and plant products (with some exemptions) without an import declaration.

See 16 USC § 3372.

Violations of the Lacey Act carry serious penalties for companies and individuals. In addition to civil fines and forfeiture of goods, criminal penalties may also attach to individuals or companies found to have knowingly and, in some cases with lack of due care, violated the Lacey Act.

A misdemeanor violation of the Lacey Act, punishable by one year in prison and a fine of \$100,000 (\$200,000 for companies), may be found if, in the exercise of due care, the individual or the company should have known the wood it purchased was illegally taken, possessed, transported or sold. Knowing of violations of the Lacey Act can lead to felony charges, punishable by five years in prison and a \$250,000 (\$500,000 for companies). See 16 USC § 3373.

The Lacey Act is not limited to direct importers of wood products. The Lacey Act broadly prohibits a company from selling, acquiring or transporting products that were illegally taken under foreign law. The definition of plant contained in the Lacey Act broadly implicates essentially every commercial wood product. This definition is applicable to manufacturers, wholesalers, distributors and even construction companies utilizing wood products in their building materials.

A Path to Compliance

The most effective way for companies to manage their risk against potential Lacey Act violations is to implement structured compliance programs that establish policies and procedures for procurement personnel, a means of reporting violations of those procedures, routinized training, as well as periodic audits of the compliance process. Absent such provisions, companies that are selling, importing, buying wood or manufacturing with wood products are at risk for government investigation and enforcement actions.

The overarching standard for Lacey Act compliance is “due care.” Stated another way, companies must make objectively reasonable efforts to ensure that their wood products are being legally sourced and transported. While the definition of “reasonable” is murky in this developing area of the law, at a minimum, compliance should include due diligence of the suppliers, an inquiry of the supply chain to the forest level, inquiry into the foreign law applicable to the supply chain and documentation of the compliance efforts. In

addition, the compliance program should include elevated levels diligence if any hot spot regions or wood species are implicated and a system for procurement personnel to identify such higher risk products.

Importers of record must also make reasonable efforts to ensure that the information contained on the import declarations, including the identification of the wood species, is accurate. Notably, criminal liability only attaches for knowingly false import declarations. Willful blindness to potential red flags may, however, be sufficient to satisfy this standard.

Additional Considerations

In addition to Lacey Act compliance, companies that are sourcing and manufacturing in foreign markets should also consider compliance efforts aimed at:

- Foreign Corrupt Practices Act and anti-bribery issues;
- Sanctions administered by the Office of Foreign Assets Control;
- Child and forced Labor prohibitions;
- Product safety (mainly for children's products);
- FTC labeling requirements (typically for leather products);
- General customs and border requirements; and
- Applicable state and local laws.

The authors of this alert represented Gibson Guitar in its high-profile Lacey Act dispute with the U.S. Department of Justice, ultimately resulting in a modest fine to Gibson and the requirement of an improved compliance plan. The authors have also advised companies on implementing proactive Lacey Act compliance strategies as a pre-emptive measure to ward off Lacey Act investigations or prosecutions.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

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