
Feds' Reliance on Environmental Activism Underscores Need for Lacey Act Compliance

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The search warrant recently executed by U.S. Customs and Fish and Wildlife Service agents on a Virginia-based flooring wholesaler surrounded allegations that the company had illegally imported wood in violation of the Lacey Act, 16 USC § 3371 et seq. It now appears that the federal investigation preceding this raid on two separate locations of the flooring company was based, in part, on an investigation conducted by an independent environmental activist group. This development bolsters three significant trends in Lacey Act enforcement that companies engaged in the purchase, manufacture or sale of wood products should take note of.

First, the Virginia raid demonstrates a continued willingness by federal enforcement agencies to rely on investigations conducted by third-party activist groups as a basis for initiating a government investigation and supporting probable cause determinations. For example, just days after federal agents raided the Virginia-based flooring wholesaler, the activist group Environmental Investigation Agency ("EIA") released a 64-page report detailing its three-year investigation into the wood buying activities of the Virginia company. The investigation identified a Chinese supplier of the flooring company and allegedly traced the origin of the wood being supplied to an allegedly protected forest in Eastern Russia that is known to be one of the last habitats of Siberian Tigers. The report referenced recorded conversations allegedly inculcating the flooring company, as well as a raft of other information that had been collected pursuant to the investigation by this independent activist group.

As reported by *The Wall Street Journal*, EIA provided the results of its findings to government authorities in advance of the flooring company raid. EIA has also been linked to the 2009 and 2011 raids on Gibson Guitar over the disputed legality of certain wood or wood products allegedly originating in Madagascar and India. Gibson denied liability and reached a favorable settlement with the United States Department of Justice and the United States District Attorney's office for the Middle District of Tennessee. Nonetheless,

Gibson's CEO has publically stated that the government investigation cost Gibson \$2-3 million and loss of untold productive personnel hours.

EIA is not the only organization engaged in such activities. Companies should be wary of this type of activism, which is not required to meet law enforcement standards, but is increasingly being used as a proxy for government investigators. Investigations conducted by individuals and activist groups, such as EIA, also are not bound by any extra-territorial jurisdiction limitations that U.S. law enforcement agencies would encounter. The impact of this is noteworthy because it effectively expands the geographic scope and capabilities of federal enforcement agencies that are willing to rely on this type of investigation to support probable cause determinations.

Second, the raid demonstrates that 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 they require a company to exercise due care in its supply chain, even if it is not the importer of record.

Finally, unlike past high-profile Lacey Act investigations, which focused on exotic and potentially threatened species (as was the case with the Gibson investigation), the focus of the Virginia raid was on common hardwoods used in everyday flooring materials. Accordingly, the belief that a company may be insulated from Lacey Act issues because it only deals 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 fact that a hedge fund has publically taken aim at the Virginia flooring company and urged its investors to short the stock, forecasting a 44 percent decline. While the flooring company disputes the forecast and challenges the assumptions upon which it is based, the company felt compelled to respond in public to the hedge fund and to address potential investor concerns directly. Disgruntled shareholders have since sued the company in a securities class action after the price of the company's stock dropped.

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. Felony culpability, punishable by five years in prison and a \$250,000 (\$500,000 for companies), may lie for knowing violations of the Lacey Act. 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 or manufacturing with wood products are at heightened 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, transported and imported. 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 of 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:

- Similar requirements under foreign laws, such as the EU Timber Regulation;

- 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);
- Formaldehyde emissions requirements (for wood products);
- Customs and import requirements; and
- Applicable state and local laws.

Pillsbury represented Gibson Guitar in the government investigation and ultimate settlement of alleged Lacey Act violations surrounding Gibson's import of wood and wood products.

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

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