

## Keep Forced Labor Out Of Supply Chains As Scrutiny Rises

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The focus on forced labor in U.S. supply chains has become more intense in the last few years and recently has garnered the attention of policymakers. Additionally, heightened scrutiny from multiple federal agencies, including U.S. Customs and Border Protection, has led to a significant increase in enforcement actions, most notably the issuance of withhold release orders, or WROs, effectively preventing the imported goods from entering the U.S. if suspected of being produced by forced labor.

CBP has specifically targeted imports from countries with allegations of forced labor, including China and Malaysia, with the majority of WROs imposed on Chinese entities.[1] The apparel industry has been heavily targeted, but CBP has also increased enforcement action across a broader range of industries, such as agricultural, seafood and electronics.

With additional U.S. legislation on the horizon, now is the time for importers to assess how they are positioned to identify and prevent forced labor in their supply chains. This article discusses the evolution of U.S. forced labor legislation and enforcement, explores several recent WROs, and identifies potential controls importers can implement to mitigate the financial risks and supply chain disruptions associated with the enforcement of regulations to combat forced labor.

### By the Numbers

With increasing pressure to eradicate forced labor, CBP enforcement actions have increased tremendously. In 2020 alone, CBP issued a number of WROs and one finding. As of March 2021, one new finding was issued determining a Malaysian disposable glove manufacturer produced goods with forced labor.[2]

Further, refuting a WRO is difficult. In March, following issuance of a WRO, CPB rejected Dandong Huayang Textiles & Garments Ltd.'s third-party audit report claiming that the goods were not produced by North Korean nationals.[3]

The charts below show the respective countries' percentage share of active WROs and the progression



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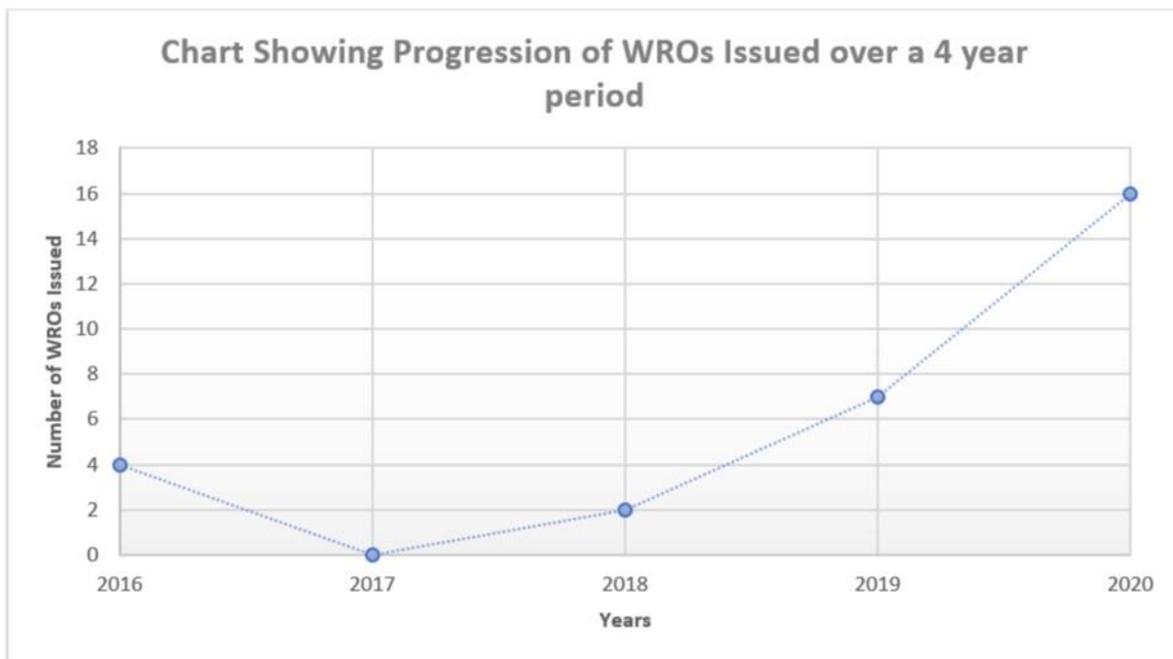
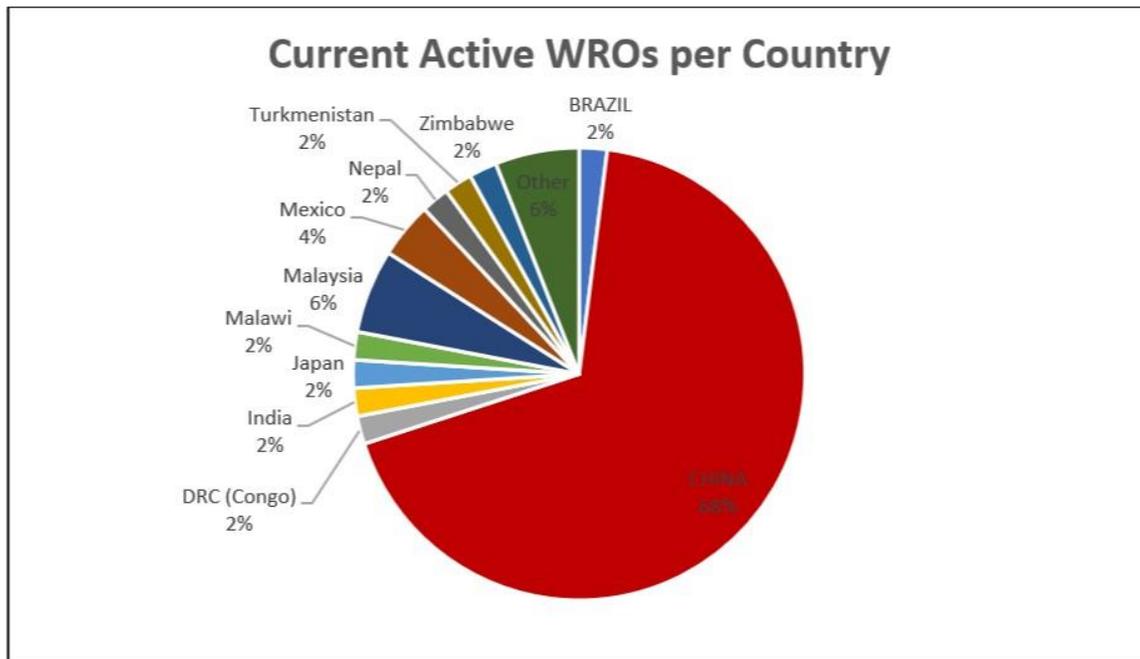


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of WROs issued by CBP over a four-year period, based on information CBP has made available.



#### How We Got Here

Prohibitions against importing goods produced with forced labor have long been a part of U.S. law.

Specifically, Title 19 of the U.S. Code, Section 1307, enacted in 1930, provides:

[G]oods produced, or manufactured wholly or in part in any foreign country by convict labor or/and forced labor or/and indentured labor under penal sanctions shall not be entitled to entry at any of the ports of the U.S., and the importation thereof is prohibited.

As a result, in situations where there is evidence or even suspicion of forced labor, the products may be denied entry.

The forced labor prohibition includes products made with indentured child labor or any work "exacted from any person under the menace of any penalty for its nonperformance and for which the worker does not offer himself voluntarily." [4] Recently, more legislative action has been taken around ensuring that forced labor is not present in supply chains, while CBP has stepped up enforcement actions. [5]

In 2017, the U.S. enacted the Countering America's Adversaries Through Sanctions Act, or CAATSA, in a step toward eradicating imports produced with forced labor, specifically targeting North Korean imports. CAATSA created the presumption that imported goods from North Korea were manufactured with forced labor. [6]

CAATSA opened the door for additional legislation to prevent imports of goods made from forced labor into the U.S. market. In June and July 2020, the U.S. government passed a series of laws and actions allowing the U.S. government to impose financial sanctions and other punitive measures.

The Uyghur Human Rights Policy Act [7] and the Xinjiang Supply Chain Business Advisory [8] detail the potential for human rights abuses when conducting business in the Xinjiang region. While the advisory does not impose new laws, it cautions that human rights violations may occur that could lead to U.S. government sanctions, and identified certain at-risk sectors.

On Dec. 2, 2020, CBP announced the imposition of a WRO on all shipments containing cotton or any cotton productions originating from the Xinjiang Production and Construction Corps, its subordinates and affiliated entities, as well as any products made in whole or in part with, or derived from, that cotton. [9] Given that approximately 80% of China's overall cotton production is from the Xinjiang region this will likely have a resounding impact on U.S. companies. [10]

### **On the Horizon: Increased Enforcement and Additional Proposed Regulations**

CBP's WRO issuance has dramatically increased. An importer who receives a WRO must export the products or run the risk of having CBP seize the products if it is unable to provide substantial evidence proving that the products were not made from forced labor.

For unprepared companies, receiving a WRO can be costly — especially if compounded with fines. In August 2020, CBP announced that PureCircle USA Inc., an importer of stevia extract from China, paid \$575,000 in penalties for imports allegedly made with forced labor. [11]

This was the first instance in which CBP collected penalties linked to a civil enforcement action regarding the importation of goods produced with forced labor. However, it likely will not be the last.

The negative impact of failing to proactively uncover forced labor in an importer's supply chain may increase throughout 2021, as awareness of the issue grows in the U.S.

Two bills that were recently introduced in Congress, the Uyghur Forced Labor Prevention Act and the Uyghur Forced Labor Disclosure Act, if passed, will require companies to more thoroughly understand their supply chains in relation to Xinjiang. [12] The proposed legislation calls for greater transparency in global supply chains, specifically requiring that publicly traded companies with activities in the Xinjiang region periodically report their activities to the U.S. Securities and Exchange Commission.

## Managing Forced Labor Risks

Title VI of the North American Free Trade Agreement Implementation Act, also known as the Customs Modernization or Mod Act, requires that parties exercise reasonable care when importing goods into the U.S.[13]

More specifically, the Mod Act mandates that importers use reasonable care when creating an entry by filing such information as is necessary to enable CBP to determine whether the merchandise was imported in accordance with U.S. trade law and may be released into U.S. commerce.

In many ways, identifying the use of forced labor can be much more complex than the information typically reported on a customs entry. For example, the importer may not have the data available to identify suppliers with heightened forced labor risk, or the supplier may not be fully transparent or cooperative.

Further, the importer is responsible for ensuring that forced labor is not present at any stage of the supply chain — including the initial sourcing of raw materials.[14] This may be a near-impossible task for multinational companies with even the most sophisticated supply chain departments.

Companies must now expand their understanding of how their suppliers obtain the necessary production inputs. It is no longer enough merely to turn raw material-sourcing activities over to the manufacturer.

In addition, while many companies have culture statements requiring that suppliers do not use forced labor, this alone is unlikely to be acceptable as proof of reasonable care during a CBP audit.

Although proactively addressing the use of forced labor presents novel challenges, not doing so may result in significant supply chain disruption — and taking back control over your imports once they are detained is not straightforward. Per Title 19 of the Code of Federal Regulations, Section 12.43, in order to refute a WRO, an importer must be able to show:

that he had made every reasonable effort to determine the source of the merchandise and of every component thereof and to ascertain the character of labor used in the production of the merchandise and each of its components, the full results of his investigation, and his belief with respect to the use of the class of labor specified in the finding in any stage of the production of the merchandise or of any of its components.

Refuting a WRO is not an easy task, as evidenced by the steps PureCircle took in responding to CBP's 2016 WRO. PureCircle provided the following documentation in response to the WRO:[15]

- A third-party audit report on the supplier's labor practices;
- A statement in PureCircle's Global Labor Policy and Supplier Code of Conduct stating the company "explicitly prohibits the use of forced labor in any part of our business"; and
- A number of detailed records, which included "purchase, production, and financial documentation, to establish clear and continuous oversight of fair labor practices throughout our supply chain." [16]

Four years after the original WRO was issued, CBP reached a settlement agreement with the company. Although PureCircle publicly stated it "did not admit any liability as part of the settlement" and it "vigorously contested the claims raised in those notices and submitted additional information to CBP to again establish forced labor was not used to manufacture [their products]"[17], CBP ultimately concluded that PureCircle failed to meet the standard for refuting an allegation.[18]

Regardless of whether a WRO is issued, the long-term reputational harm to a company resulting from forced labor allegations can be significant. For example, in 2018, the Associated Press released a report claiming allegations of forced labor in Badger Sportswear's supply chain.[19] Badger Sportswear is an apparel company that primarily sells sportswear to colleges. As a direct result of the forced labor allegations, many colleges removed Badger Sportswear from their stores.

### What a Company's Program Should Look Like

A multipronged effort is needed to identify the presence of and to prevent forced labor in a supply chain. Although CBP has not issued formal requirements, it has provided guidance around successful mitigation strategies.

CBP's forced labor due diligence guidance publication provides that a reasonable care framework should include the following elements:[20]

| Phase 1 - Risk Mitigation |  |
|---------------------------|--|
| 1                         | Engage Stakeholders & Partners                 |
| 2                         | Assess Risks & Impacts                         |
| 3                         | Develop Code of Conduct                        |
| 4                         | Communicate and Train across your Supply Chain |

| Phase 2 - Internal Compliance |                      |
|-------------------------------|----------------------|
| 1                             | Monitor Compliance   |
| 2                             | Independent Review   |
| 3                             | Remediate Violations |
| 4                             | Report Performance   |

An integral component of this framework is building a corporate culture focused on ethical behavior and values. Establishing a strong tone at the top that use of forced labor is not tolerated encourages employees to speak up when they identify possible signs of forced labor.

A zero-tolerance forced labor position should be supported by a defined governance structure composed of trade compliance, supply chain, sourcing and legal, with oversight from leadership.

The governance structure should implement and enforce standardized processes as well as written codes of conduct, policies and procedures to facilitate compliance and ethical behaviors in supply chain sourcing. This may include requiring the provision of supporting documents related to upstream suppliers.

A code of conduct is a good place for most companies to begin planning out what their program will look like, as it is the backbone of an effective ethics and compliance framework. According to the U.S. Department of Labor:

A good code of conduct should be a public document and state clearly the actors within the company that are responsible for its development, oversight and implementation which should include the Board of Directors and senior management, as well as all of the business units involved in social compliance.[21]

As a leading practice, many companies keep their supply chain code of conduct on the company's website to make it publicly accessible. It should be supported by standard operating procedures that outline the proactive steps the importer takes in order to mitigate forced labor risks, including a defined escalation process.

Once a framework is in place, importers should develop measurable milestones to help identify risks in their supply chains. A potential milestone includes increasing supply chain transparency by utilizing data analytics and automation — e.g., blockchain — to conduct supply chain mapping.

Supply chain mapping should identify manufacturer names, cities, countries and products. Importers should also document sourcing procedures among its manufacturers to limit potential use of forced labor at the raw material level.

Another key element is documenting common ownership among manufacturers or suppliers. This enables importers to identify potentially problematic related entities. If a related entity is identified as having forced labor, the importer should then conduct a thorough risk assessment of its supply chain against the DOL's forced labor lists, CBP's WRO lists, and trending forced labor risks identified by nongovernmental organizations or the media.

Once finalized, this assessment should provide a comprehensive, prioritized overview of the enterprise's risks.

The following example shows what a risk assessment may look like.

On Sept. 30, 2020, CBP identified a Malaysian company alleged/suspected to use forced labor to manufacturer palm oil.[22] In even a high-level risk assessment, the WRO would be used to flag the following data elements as potential risks: country of origin, manufacturer name and product. Based on the level of perceived risk, or overlapping data points, the importer will then be able to determine next steps.

Potential scenarios include:

- Scenario 1 — Medium Risk: The data analysis shows that the importer is sourcing palm oil from Malaysia but not from the targeted manufacturer. Next steps may include: (1) sending questionnaires to the identified factories to assess their relationship with identified manufacturers; and (2) monitoring and testing Malaysian factories supplying palm oil to ensure forced labor is not being used.
- Scenario 2 — High Risk: The data analysis shows that the importer is sourcing palm oil from a Malaysian factory identified by the WRO. Next steps may include determining if the factory is a complete match to the factory listed in the WRO, conducting a thorough investigation and potentially placing a hold on shipments from the factory until the forced labor issue has been remediated. A remediation plan includes obtaining evidence that the supplier's labor practices

have changed and no longer utilize forced labor or that the importer is no longer purchasing from the supplier.

To accomplish their objectives, companies should consider implementing independent third-party audits, since it is unlikely that most factories are willing to disclose the use of forced labor to their customers, and detecting forced labor requires experience conducting data-driven and onsite assessments, where possible.

A third-party audit should involve, at a minimum, an auditor that is unrelated to the importer and factory, minimal oversight from the importer or factory, and the opportunity to conduct unannounced on-site inspection and testing. The on-site testing should include confidential interviews with factory workers, conducted in the same language as the workers, and home visits to assess living conditions.

Although difficult to perform, home visits are an important piece of the audit and should be conducted when possible as they will assist in identifying inhumane living conditions on the factory's property — e.g., unventilated shipping containers.

Additional forced labor risk indicators include, but are not limited to:

- Workers that appear to be younger than the legal age limit;
- Working conditions that appear unsafe — e.g. the building does not appear to be structurally sound, inadequate ventilation, insufficient number fire exits, etc.;
- Overcrowded working conditions;
- Unreasonable on-site living conditions;
- Workers are not provided breaks and/or the number of hours worked seems above the legal limit for the jurisdiction;
- Payroll and time records appear to be tampered with or do not indicate a legal wage; and
- Management appears to hold legal identification documents for employees, such as an employee's immigration documents

As a final control, importers should conduct training for appropriate personnel to sensitize them to forced labor warning signs, and develop steps to disclose and remediate potential issues. It should also include awareness training for manufacturers to ensure they are sensitized to the use of forced labor and the ramifications for using it.

Tailoring CBP's framework for the particular nuances of the importer's industry will facilitate managing forced labor risks. Understanding risk drivers in specific industries and developing a plan to address them will help companies avoid both costly WROs and negative public perception.

### **Guidance on WRO Revocation Process**

In March 2020, CPB released guidance for importers addressing the revocation process, should an importer be presented with a WRO.[23] The process highlights four different components:

1. The petitioner submits information to CBP;
2. CBP and the petitioner engage in a remediation dialogue;
3. CBP determines whether the International Labor Organization indicators are remediated; and
4. CBP modifies or revokes the WRO based on the determination.

Importers may consider gathering supporting documentation for shipments from high-risk regions. Having this documentation on hand will facilitate release in the event goods are detained — the challenge for importers with detained goods is often gathering the necessary information in a reasonable time.

Developing a process to identify and escalate potential at-risk shipments can help importers navigate a difficult release process.

## **Conclusion**

With the increasing scrutiny and enforcement to combat forced labor practices, along with proposed legislation increasing regulations to which companies may be subject in the future, it is imperative that companies prepare for these risks. The penalties for noncompliance are likely to increase while the reputational harm of using forced labor could have a devastating impact on a company's brand.

During this period of intense financial pressure on companies already facing steep importing tariffs, companies continue to seek low-cost overseas production and many are seeking sourcing changes for their imported goods. But importers should be aware of these underlying risks as they evaluate suppliers.

Fully understanding the supplier's sourcing and production structure may prevent long-term challenges. Developing and implementing a strong, auditable compliance program will help an enterprise position itself to be a responsible, compliant importer.

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[1] As of October 2020, nine of the 13 WROs issued in 2020 were imposed on Chinese entities.

[2] 16380 Federal Register / Vol. 86, No. 58 2021-06393.pdf, <https://www.govinfo.gov/content/pkg/FR-2021-03-29/pdf/2021-06393.pdf>.

[3] H317249, CROSS Customs Rulings Online Search System, <https://rulings.cbp.gov/search?term=H317249&collection=ALL&sortBy=RELEVANCE&pageSize=>

30&page=1.

[4] 48 CFR § 22.1501.

[5] See H.R.6210 - Uyghur Forced Labor Prevention Act, <https://www.congress.gov/bill/116th-congress/house-bill/6210>.

[6] Public Law 115-44, SECTION 1 (CAATSA), <https://www.congress.gov/115/plaws/publ44/PLAW-115publ44.pdf>.

[7] S.3744 - Uyghur Human Rights Policy Act of 2020, <https://www.congress.gov/bill/116th-congress/senate-bill/3744>.

[8] Xinjiang Supply Chain Business Advisory, Customs and Border Protection, (July 2020), <https://www.cbp.gov/document/guidance/xinjiang-supply-chain-business-advisory>.

[9] DHS Issues Detention Order on Cotton Products Made by Xinjiang Production and Construction Corps Using Prison Labor. Department of Homeland and Security, (December 2020), <https://www.dhs.gov/news/2020/12/02/dhs-issues-detention-order-cotton-products-made-xinjiang-production-and-construction>.

[10] UK urged to stop cotton imports made in Chinese 'prison camps', Reuters, (April 2020), <https://www.reuters.com/article/us-britain-cotton-china-trfn-idUSKCN225016>.

[11] CBP Collects \$575,000 from PureCircle USA for Stevia Imports Made with Forced Labor, U.S. Customs and Border Protection, (August 2020), <https://www.cbp.gov/newsroom/national-media-release/cbp-collects-575000-pure-circle-usa-stevia-imports-made-forced-labor>.

[12] The Uyghur Forced Labor Prevention Act and the Uyghur Forced Labor Disclosure Act of 2020.

[13] Pub. L. 103-182, 107 Stat. 2057.

[14] Responsible Business Practices on Forced Labor Risk in the Global Supply Chain, Customs and Border Protection (2020), [https://www.cbp.gov/sites/default/files/assets/documents/2018-Aug/CBP%20Responsible%20Business%20Practices%20on%20Forced%20Labor\\_v4%20%28FINAL%20with%20Publication%20Number%29.pdf](https://www.cbp.gov/sites/default/files/assets/documents/2018-Aug/CBP%20Responsible%20Business%20Practices%20on%20Forced%20Labor_v4%20%28FINAL%20with%20Publication%20Number%29.pdf).

[15] PureCircle and U.S. Customs and Border Protection Resolve 2014 Stevia Sourcing. Pure Circle (August 2020), <https://purecircle.com/news/purecircle-and-u-s-customs-and-border-protection-resolve-2014-stevia-sourcing/>.

[16] Commerce Department Adds Eleven Chinese Entities Implicated in Human Rights Abuses in Xinjiang to the Entity List, U.S. Department of Commerce, (July 2020), <https://www.commerce.gov/news/press-releases/2020/07/commerce-department-adds-eleven-chinese-entities-implicated-human>.

[17] CBP Collects \$575,000 from Pure Circle USA for Stevia Imports Made with Forced Labor, U.S. Customs and Border Protection, (August 2020), <https://www.cbp.gov/newsroom/national-media-release/cbp-collects-575000-pure-circle-usa-stevia-imports-made-forced-labor>.

[18] CBP Issues First Forced Labor Finding Since 1996, CBP (2020), <https://www.cbp.gov/newsroom/national-media-release/cbp-issues-first-forced-labor-finding-1996>.

[19] U.S. Sportswear traced to factory in China's internment Camps, Associated Press, (December 2018), <https://apnews.com/article/99016849cddb4b99a048b863b52c28cb>.

[20] Fact Sheet: Responsible Business Practices, CBP (2020), <https://www.cbp.gov/document/fact-sheets/fact-sheet-responsible-business-practices>.

[21] Combatting Forced Labour, A Handbook for Employers & Business, International Labour Organization, (2015), [https://www.ilo.org/wcmsp5/groups/public/---ed\\_norm/---declaration/documents/publication/wcms\\_101171.pdf](https://www.ilo.org/wcmsp5/groups/public/---ed_norm/---declaration/documents/publication/wcms_101171.pdf).

[22] CBP Issues Detention Order on Palm Oil Produced with Forced Labor in Malaysia, <https://www.cbp.gov/newsroom/national-media-release/cbp-issues-detention-order-palm-oil-produced-forced-labor-malaysia>.

[23] WRO MODIFICATION/REVOICATION PROCESS Overview, Customs and Border Protection, CBP Publication 1394-0321, March 2020.