



Timber Trade Federation  
growing the use of wood

DUE DILIGENCE | BUILDING UNDERSTANDING  
ARTICLE ONE, SEPTEMBER 2020

# WHAT DOES DUE DILIGENCE LOOK LIKE?

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## INTRODUCTION

Due Diligence as a form of supply chain management to address illegal logging and deforestation is back in the public spotlight as legislation is now being proposed for a range of ‘forest risk’ commodity companies trading soy, palm oil, beef and other goods which can originate in areas where forest land has been illegally cleared for agriculture.

Timber is a forerunner when it comes to this sort of due diligence and there is a lot which firms can learn from our industry including what due diligence looks like.

Legislation to tackle illegal logging under the EU Timber Regulation (EUTR) has been in place since 2013, and will continue through the UK Timber Regulation when the UK leaves the EU. However, Due Diligence does not stand still, and NGO’s, firms and regulators all seek improvements.

Forest Trends in [their latest report summarising 10 lessons learned from the EUTR](#) noted that while the term Due Diligence “has a traditional legal sense of having gathered and considered all evidence necessary to be confident”, it often continues to be confused with simple ‘paperwork’.

Firms can often be further confused because Due Diligence is inherently a subjective process, without one set universally agreed approach, and has uneven requirements across jurisdictions and legal systems. However, there are certain objective elements which can be observed in a Due Diligence process.



### Why is Due Diligence confused with paperwork?

There is a misconception that Due Diligence equates to ‘paperwork’, such as permits. While it is true, compared with non-tangible information, such as industry insight and supplier engagement activities, paperwork is the most ‘presentable’ type of input and output, but it is not the full package of Due Diligence.

Paperwork, whether permits or customs slips are much easier to be passed around, understood by, and presented as evidence. However, it is only when supported by checks and follow up actions to which round out the reasoning by a firm that a product represents a ‘Negligible’ risk conclusion, paperwork can be deemed as evidence of Due Diligence.

This can be a challenge for many SMEs who often do not have the capacity, of time, human capital, or technical expertise, to tell the entirety of their train-of-thoughts behind their buying decision, and may rely on paperwork as the ultimate evidence of their actions.

### Then what does Due Diligence look like?

If you were to break Due Diligence down (as we have done in Figure 1 below), you can see this system operates on a stream of information and action inflow (I), which follows a set of pre-defined criteria (X) and processes (Y), and generates an output (O). In timber these can be seen as the below:

- **I, the Input:** the array of soft and hard information about the product, its supply chain, and other sector insight obtained via the variety of activities, from desktop research to supplier engagement, stakeholder dialogue to scientific testing.
- **X, the Criteria:** list of categories for exploring potential risk as defined by the Timber Regulation and its official guidance, and any other sources or risk factors companies should take into consideration during the subsequent processes.
- **Y, the Process:** the iterative process of assessment, mitigation, implementation, and monitoring.
- **O, the Output:** the final risk level of the product, i.e. non-negligible or negligible risk.

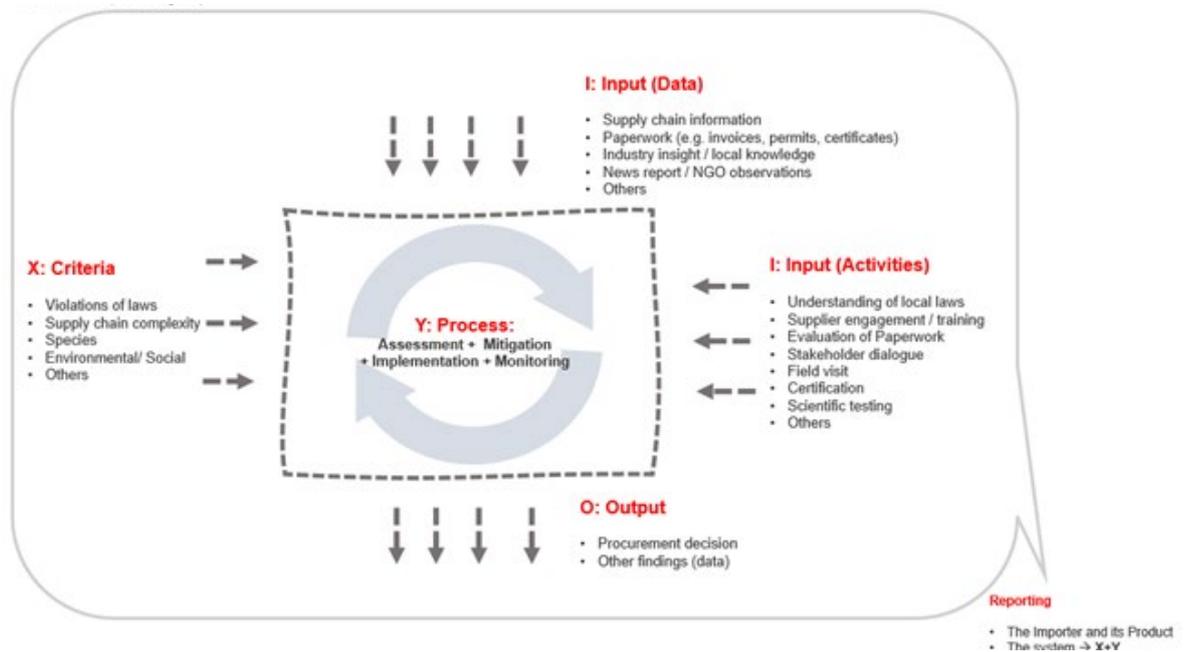
To demonstrate evidence of this lengthy process of Due Diligence for any timber product to a downstream client or the third-party auditors, companies need to be able to explain their decision-making process reaching the final O. This means a key component of Due Diligence is reporting.

Reports must be written in a way that can be easily understood, and comprehensive, to communicate the intricacies of thinking involved. This is essential, both as evidence of



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ARTICLE ONE, SEPTEMBER 2020



Due Diligence, and to demonstrate your interpretation and evaluation of risks that is applicable to your product supply chain

While I, O, X, Y, and Reporting may describe the objective elements of Due Diligence, there remain questions on the depth of the input data, the width of actions required, and the timing and conditions to trigger an action. Can these dynamic properties also be determined systematically?

The concept of Due Diligence is based on the decision-making of a ‘reasonable individual’, and the perceptions of what constitutes ‘reasonable’ varies extremely widely among NGOs, companies, regulators, and lawmakers (Forest Trends).

One of the ultimate objectives of the Timber Regulation is to ensure companies take responsibility for their own actions. Business need to actively look into the sources of their timber to make their own assessments and show that they have done so.

To make this work, companies required to exercise Due Diligence will also need the support from industry stakeholders including independent NGOs and forest monitors. This is not only about exchange of information on risks but to support the ‘translation’ of risks into actionable and sustainable mitigation measures on the ground.

Be it the sharing of insight about a region or company, or guidance on how to evaluate a piece of paperwork, after all, Due Diligence is beyond the vertical interaction of players along the supply chain, it is a horizontal exercise across the industry too.



### Where gaps in Due Diligence could exist

Gaps could exist in each of the components, and manifest in a variety of forms:

- **X, the Criteria** - Completeness and the correct interpretations of key risk categories as required by the Regulation. For example, lack of consideration on risks of mixing in composite products.
- **I, the Input** - Information accuracy and reliability; For example, paperwork showing contradicting information; Action suitability and effectiveness; For example, insufficient sampling approach or wrong testing methodology; failure to check stakeholders' observation of legal violation related to the product supply chain.
- **O, the Output** - Consistency of risk conclusion with justification and evidence.
- **Reporting** - Timeliness and adequacy of the report to demonstrate processes and actions taken, and their output.

Gaps could also exist if the system itself is not being implemented consistently across all products, or is not being maintained within the company, e.g. lack of knowledge continuity among old and new staff, poor file management, etc.

### Areas for future improvement

There is a wide range of information sources and platforms in the public domain that helps companies with different components of due diligence. However, it is up to the company to put them together and make it work.

We recently launched a Due Diligence Toolkit to assist Operator companies with their work. The Toolkit is developed based on the understanding of X-Z and aims to capture some of the commonly occurring gaps in companies' due diligence.

The Toolkit present key due diligence stages (Z) in an interactive flow chart. Each box in the flow charts represents a category of assessment criteria (Z/Y) as defined by the Timber Regulation and contains a list of common risk factors companies should be considering (X) and options on mitigation actions companies may need to be using (X). Users can directly enter their responses and list of information in the space provided and save the document as final report (reporting).

The Toolkit serves as a guidance for conducting due diligence and aims to encourage companies examine their own existing procedure to ensure key criteria, risk factors,



stakeholder information, and mitigation actions are not being missed during their process. It also aspires to encourage better reporting of companies on the full range of their input and actions taken, beyond just ‘paperwork’.

As UK companies prepare for conducting Due Diligence for timber products imported from the EU mainland, this Toolkit is aimed to also help new Operators to get on board and ensure that they have the minimum tools to deliver the requirements.

From 1 Jan 2021, all UK businesses importing timber from the EU/EEA and outside will be classified as Operators and are required to carry out Due Diligence under the UK’s timber legislation, and vice versa under the EU Timber Regulation.

TTF has embedded mandatory Due Diligence as part of its membership policy and requires all operator members to go through an annual audit on the quality of their Due Diligence process and outcome.

## Next steps

We understand that this Toolkit is not going to capture all the possible risks and legal violations out there, but we will continue to review and improve the Toolkit to ensure it is up to date with the latest industry guidance and best practice.

We welcome comments and suggestions from industry stakeholders, so please do email us at [ttf@ttf.co.uk](mailto:ttf@ttf.co.uk), and make sure to [download the toolkit](#), shown below.

