Canada targets supply chain ethics

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The Government of Canada is reacting to growing consumer and political support to combat forced labour and human rights abuses in supply chains by implementing new laws and policies. As a result, Canadian companies are under pressure to address the issue of human rights abuses and to comply with new and developing domestic and foreign legislation targeting supply chain ethics.

Current developments under the Canadian legal landscape include:

- Heightening scrutiny of goods manufactured in the Xinjiang Uygyr Autonomous Region (XUAR) of China;
- The Canadian Ombudsperson for Responsible Enterprise's (CORE) publication of its complaint procedures, its initiation of an investigation into the Canadian apparel industry and its initiation of non-review country visits; and
- The introduction in the Senate of two bills aimed at stopping forced labour: Bill S-204, *Xinjiang Manufactured Goods Importation Prohibition Act*[1] and Bill S-211, *Fighting Against Forced Labour and Child Labour in Supply Chains Act*.[2]

In response to these developments, Canadian businesses must address the shifting legal landscape and ensure that their compliance policies properly reflect advancements under Canadian law concerning prohibitions on forced labour, supply chain reporting mechanisms and the operation of the CORE. We expect that Canadian laws, policies and enforcement initiatives will continue to develop regarding identifying and preventing the import of goods produced with forced labour and policy initiatives to combat the use of forced labour around the world.

Reporting obligations on preventing forced labour in supply chains

In a fourth attempt to legislate on modern slavery, Bill S-211 was introduced in the Senate on Nov. 24, 2021.[3] The Bill passed in the Senate and is currently before the Standing Committee on Foreign Affairs and International Development (SCFAID) in the House of Commons.

Similar to its predecessors, Bill S-211 aims to combat modern slavery by imposing supply chain reporting requirements on businesses. The April 6, 2022 report issued by

the Standing Senate Committee on Human Rights recognized that Bill S-211 alone will not solve the problem of forced labour and child labour in the world. The report encourages the Government of Canada to adopt the bill as a starting point.

Given the federal government's commitment to the conventions of the International Labour Organization on fundamental labour rights, it seems likely that the government will prioritize passing the fourth iteration of this legislation and follow the examples set by the United Kingdom (*Modern Slavery Act 2015*) and Australia (*Commonwealth Modern Slavery Act 2018*).

Canadian businesses should review the draft legislation and consider the following:

- Whether they meet the proposed definition of an "entity";
- Whether their compliance policies guard against the use of forced and child labour in their supply chains; and
- What measures should be implemented to address reporting requirements under Bill S-211.

If passed in its current form, Bill S-211 will apply to all entities (and related controlling entities) that produce or sell goods in Canada (or elsewhere) and/or import goods into Canada. "Entity" is defined as a corporation, a trust, a partnership, an organization listed on a Canadian stock exchange, an organization prescribed by regulation, and an organization that operates (i.e., is located, carries on business, or holds assets) in Canada. To be considered an entity, the previous two years of financial statements must meet two of the following factors: $20 million in assets, $40 million in revenue or at least 250 employees.

An entity's sole obligation under Bill S-211 is to prepare an annual report on its measures in place to prevent and reduce the risk that forced labour or child labour was used to produce or import goods into Canada.

The entity's governing body must approve the annual report and directors and federal corporations (incorporated under the *Canada Business Corporations Act*) must distribute the annual report to its shareholders with its audited financial statements. Entities are liable for acts by employees, agents, or mandataries unless they exercised due diligence to prevent its commission and officers face party liability. The offence provisions provide for the potential to levy fines of up to $250,000.

Although the Canada Border Services Agency (CBSA) already has the authority to detain goods on the suspicion of forced labour and prohibit goods from entering Canada if an investigation confirms their suspicions, Bill S-211 creates the first legislated structure for corporate compliance on preventing the use of forced and child labour to manufacture goods imported into Canada.

Prohibition on goods entering Canada manufactured with forced labour

To comply with requirements under the Canada-United States-Mexico Agreement (USMCA), Canada amended provisions under the *Customs Tariff* (tariff item No.

9897.00.00) to prohibit the importation of goods mined, manufactured or produced wholly or in part by forced labour.

The CBSA works with the Labour Program of Employment and Social Development Canada (ESDC) to enforce this prohibition. The CBSA uses information from ESDC reports on problematic supply chains to identify, detain, and inspect goods pursuant to its authority under the *Customs Act*. The ESDC report on Labour Exploitation in Global Supply Chains includes the recommendation that Canada implement mandatory human rights due diligence mechanism.

The Federal Court recently dismissed an application where the applicants argued that CBSA has authority to implement a "presumptive determination" on all goods imported from the XUAR on the basis that the goods have an increased likelihood of being produced using forced labour.

The applicants argued that the CBSA should apply a reverse onus to goods manufactured in XUAR: prohibiting importation unless an importer provides clear evidence that the goods were not manufactured with forced labour. The CBSA's position is that goods must be classified on a case-by-case basis consistent with the Harmonized System on which tariff items are based, that classification must be defensible to the CITT under the *Customs Act*'s administrative process, and that it can only classify goods that are identified and imported (or intended to be imported) – not hypothetical goods. The court held that the CBSA's interpretation of its authority under the *Customs Tariff and the Customs Act* was reasonable.

CBSA has the authority to re-determine the tariff classification of and detain goods produced by forced labour and can issue a notice of re-determination of tariff classification. In response, an importer can seek a further re-determination of the tariff classification by the CBSA's president within the specified legislative period. However, the appeal process may result in lengthy proceedings, with potential of a further appeal to the Canadian International Trade Tribunal and possibly a judicial review.

In January 2022, the CBSA revised D-Memorandum 9-1-6 to provide guidance to importers on the type of evidence an importer may submit if their goods are detained on suspicion of forced labour. This iteration of the D-Memorandum required an importer to provide documentation illustrating their complete supply chain: "the entire system of producing and delivering the goods from the initial stage of sourcing raw materials to the delivery of the product in Canada," including documentation showing origin, purchase and transportation of all materials used to manufacture the impugned goods. Revisions to the D-Memoranda in May 2022 removed this guidance. The CBSA has the D-Memorandum marked as "under review."

We expect that the CBSA will issue additional guidance on the procedural mechanisms for disputing an allegation that goods were produced by forced labour. Importers with goods detained on the suspicion of forced labour should immediately seek legal advice for navigating the CBSA's re-determination and subsequent appeal process.

Forced labour concerns in Xinjiang

A number of governments around the world have paid particular attention to forced labour concerns in the XUAR. In Canada, following evidence of forced labour in the XUAR, the federal government introduced the Integrity Declaration on Doing Business with Xinjiang Entities (the Declaration). Canadian companies sourcing directly or indirectly from XUAR or relying on Uyghur labour, are established in XUAR, or are seeking to engage in the XUAR market, must sign a Declaration before seeking support from the Trade Commissioner Service (the TCS), that is in place for five years.

The Declaration confirms the company is aware of the ongoing human rights situation in the XUAR and that the TCS expects Canadian companies to respect human rights. It also confirms the TCS will not provide support to companies knowingly engaged in conduct inconsistent with international human rights standards. The Declaration goes on to confirm that the signatory has not sourced materials from a supplier implicated in human rights abuses in the XUAR.

Following the introduction of the Declaration, in April 2021 the Government of Canada announced sanctions, the *Special Economic Measures (People's Republic of China) Regulations*, in response to the gross and systematic human rights violations occurring in the XUAR. The sanctions include a broad dealings prohibition and prohibit providing goods or financial services for the benefit of a listed person. The intended affect is to deter Canadian businesses further from dealing with entities or individuals in the XUAR.

In November 2021, Bill S-204 was introduced in the Senate. The bill seeks to amend the *Customs Tariff* by adding a prohibition on importing goods manufactured or produced wholly or in part in the XUAR. Bill S-204 is currently in its second reading in the House of Commons.

This bill aligns with Canada's obligations under Article 23.6 of the USMCA to prohibit the importation of goods manufactured with forced labour. The bill also aligns with U.S. Congress passing the *Uighur Forced Labour Prevention Act* in the summer of 2021, which applies the presumption that goods manufactured in XUAR are made with forced labour, and the U.S. Congress doubling down and banning imports from XUAR in December 2021.Prohibition took effect on June 20, 2022.

The Government of Canada has provided limited guidance on specific supply chain risks in the XUAR. However, the U.S. Department of State issued comprehensive guidance, the Xinjiang Supply Chain Business Advisory, on identifying warning signs that may indicate use of forced labour. The advisory also outlines the potential for supply chain risk in certain industries like surveillance, biometrics, tracking technology, agriculture (cotton and tomatoes), and solar technologies.

Canadian businesses whose suppliers have operations in or proximate to XUAR should review the available guidance on importing goods from this region. They should also regularly conduct supply chain audits to ensure their suppliers, including those supplying raw material inputs, are not using materials manufactured in the XUAR.

Canadian Ombudsperson for Responsible Enterprise

The CORE investigates public complaints, initiate reviews of potential human rights abuses by Canadian companies and may initiate studies. The CORE's mandate only applies to the extractive (mining/oil and gas) and apparel sectors; however, its mandate may expand over time. Our previous article provides a backgrounder on the CORE's mandate and its relationship to the UN Guiding Principles on Business and Human Rights.

Recent developments at the CORE include:

- The release of the CORE's operating procedures;
- A report suggesting that Parliament strengthen the investigative powers of the CORE;
- Its first study into child labour in the Canadian apparel sector; and
- The implementation of non-review country visits.

Operating Procedures and Complaints Portal

In spring 2021, the CORE released its operating procedures and established an online form for public complaints – the Human Rights Responsibility Mechanism (HRRM) and began to accept complaints on alleged human rights abuses by Canadian businesses operating abroad. To date, the CORE has received 46 inquiries and five complaints.

The CORE's complaint process is available on its website. The primary criteria are:

1. A complaint must concern abuse of an internationally recognized human right; and
2. The behaviour that is the subject of the complaint must have occurred outside Canada after May 2019 by a Canadian company, in the mining, garment or oil and gas industry.

The CORE's process for reviewing and resolving complaints includes the following steps:

- As part of its intake process, the CORE contacts a complainant (who may remain anonymous subject to certain considerations, such as the risk of retaliation) and determine whether their complaint meets admissibility criteria.
- The CORE makes a determination on the admissibility of a complaint and then advises the Canadian company that it is subject to a complaint.
- The CORE undertakes an initial assessment and works with a complainant and the Canadian company to resolve the offending behaviour. A complaint is not public until an initial assessment is complete.
- The CORE may facilitate a mediation between the two parties.
- The CORE may investigate the complaint and may terminate or complete their investigation and publish a publicly available report on its findings, which may include recommendations.

The CORE's authority includes making recommendations to refer the matter to arbitration, law enforcement or a regulatory agency. Failure to participate in an investigation may cause the CORE to come to negative conclusions against the subject of the complaint. All parties are required to act in good faith during an investigation, including in implementing recommendations. Failure to act in good faith may result in

the withdrawal or denial of trade advocacy support or the refusal of financial support from Export Development Canada.

The CORE considers the following five criteria when determining whether to review of a potential human rights abuse:

- Systemic (whether the possible abuse is significant because it impacts a large group of people (international, throughout an entire industry, a persistent/longstanding issue));
- Whether those affected are in underserved groups and communities;
- Feasibility of appropriateness (whether the nature of the possible abuse is appropriate for a public and participatory review process);
- Impact (whether a review will result in meaningful findings, remedies or recommendations); and
- Strategic relevance (whether the review aligns with the CORE's mandate and strategic priorities).

Report on the CORE's powers

The Standing Committee on Foreign Affairs and International Development presented a June 2021 report studying the role of the CORE and the scope of its mandate. The report recommended the federal government implement legislation that imposes human rights due diligence obligations on Canadian companies to identify, prevent, mitigate and account for adverse human rights, environmental and gendered impacts throughout their supply chain and operations. In addition, the report requests that Parliament consider tabling legislation to strengthen the investigative powers of the CORE, authorizing the CORE to compel witnesses and documents.

Child labour study in Canada's apparel sector

In December 2021, the CORE announced its first study on child labour in the Canadian apparel sector. The Terms of Reference for the study provide the CORE's objective: to examine whether and how Canadian apparel companies address the risk of child labour and ensure respect for children's rights in their overseas operations and supply chains. The CORE will interview stakeholders throughout 2022.

Non-review country visits

The CORE completed its stakeholder consultation on Non-Review Country Visits and announced it will visit countries not currently subject to a complaint through the HRRM or a CORE-initiated study. Countries chosen for visits will include with significant presence of Canadian garment, mining, and/or oil/gas companies or their subcontractors, and where Canadian companies are operating on or in close proximity to Indigenous land and territories. The CORE will publish its' intent to visit a specific country, alert key stakeholders and publish a report outlining its findings.

Takeaways for Canadian businesses: Supply chain ethics

Canadian businesses' supply chains are under increased scrutiny by the federal government. After initially holding shipments of nitrile gloves in January 2022, Public Services and Procurement Canada (PSPC) announced it terminated its existing contracts with a supplier due to serious allegations regarding forced labour. The CBSA confirmed it seized its first shipment due to forced labour concerns. However, these enforcement efforts pale in comparison to the U.S., which continues to pressure Canada to enforce its commitment under the USMCA to prohibit the importation of goods manufactured with forced labour.

Canadian businesses should continue tracking Bills S-204 and S-211 through the legislative process and review their internal compliance procedures to ensure they properly reflect the current advancements in law, with particular attention paid to new supplier onboarding and internal vetting processes when contracting with third parties. If businesses detect weaknesses in their policies and procedures they need to review their internal compliance documents, implement training with support from senior executives, and continually assess whether their policies are positively influencing behaviour through regular audits and data collection.

Canadian businesses should also examine their current supplier relationships and undertake internal audits to ensure they comply with reporting requirements, like the Xinjiang Integrity Declaration. It is also important to consider the impact of foreign forced labour and corporate due diligence laws.

In June 2021, the German parliament passed the *Act on Corporate Due Diligence in Supply Chains*, which requires certain companies to implement due diligence procedures to prevent human rights and environmental abuses in their supply chains. Canadian multinational companies may be required to comply with legislation in foreign jurisdictions.

The consequences of failing to undertake supply chain audits to ensure your business is sourcing from appropriate suppliers and conducting operations responsibly may result in possible legal action and lasting reputational damage. The contract termination by the PSPC is a noteworthy example of the current scrutiny applied to supply chains and a reminder of the potential to lose significant contracts when there is an allegation of forced labour.

With respect to the CORE, Canadian companies in the extractive and apparel sectors must consider the possibility that their operations may be the subject of a complaint or a CORE-initiated investigation, or that the CORE is visiting and reviewing a country where it has operations. If a Canadian company is the subject of a complaint, it should seek legal advice on the CORE's investigative process.

BLG can guide Canadian businesses through a supply chain audit, review internal compliance policies and standard operating procedures, provide advice on supply chain ethics, and advise on investigations undertaken by the CORE. Reach out to any of the key contacts below for assistance.

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