

The Complete Guide to Supply Chain Due Diligence in the Energy Sector

Addressing Challenges and
Implementing Effective Strategies
with Real-World Examples



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Introduction

In the fast-evolving energy sector, managing complex and demanding supply chains is more than a regulatory requirement; it's a strategic necessity. These complexities not only impact operational efficiency but also affect sustainability, costs, and risk management. Increasingly, accusations of 'greenwashing' also threaten the credibility and reputation of companies.

The world is shifting from a dependence on fossil fuels to a world where 90% of electricity generation is predicted to come from renewable sources. The UN has set out its sustainable development goals and across the business world, organisations are responding by embracing a new Environmental Social Governance (ESG) era that encompasses GHG emissions and the drive to net zero.

To support these goals, organisations globally are being swept up in a metaphorical ESG regulatory net—such as Australia's Modern Slavery Act, Canada's [Bill S-211](#), Germany's [Lieferkettengesetz](#), Norway's [Apenhetsoven](#), India's [BRSR Core](#), or the EU's forthcoming [Corporate](#)

[Sustainability Due Diligence Directive \(EU CS DDD\)](#). These regulations require companies to assess human rights and environmental risks within their supply chains and report proactively on their mitigation efforts.

Across the entire end-to-end process, from the finished product to the metals, minerals, and other raw materials required to make them, companies must now demonstrate a clear understanding of the impact they are having on people and the planet. Ethical business is not just a way to differentiate or meet increasingly discerning consumer expectations; it's a regulatory issue with significant penalties for failing to comply.

What is Supply Chain Due Diligence in the Global Energy Sector?

Supply chain due diligence in the energy sector is more than just compliance. It's about embedding responsible corporate behaviour into operations, focusing on human rights, environmental impacts, and aligning with international guidelines and energy-specific standards. In this sector, where operations often span vulnerable and diverse geographies, the need for heightened attention to human rights and environmental preservation is not just ethical but a safeguard against reputational and legal risks.

Supply Chain Due Diligence generally draws on international guidelines such as the [OECD Guidelines](#) for Multinational Enterprises, [UN Guiding Principles on Business and Human Rights](#), [human rights conventions defined by the International Labour Organisation \(ILO\)](#), and the [UN Sustainable Development Goals](#). However, it is further supplemented by energy-specific standards and frameworks that provide additional layers of scrutiny and accountability.

Real-World Example

The [Deepwater Horizon oil spill](#) serves as a stark reminder of the importance of due diligence in supply chain management. Without Due Diligence, the consequences can be catastrophic, not only environmentally but also financially and reputationally. The spill, which released millions of barrels of oil into the Gulf of Mexico, resulted in the loss of life, extensive environmental damage, and a \$65 billion financial blow to BP. This disaster highlights the need for stringent due diligence to prevent such incidents and their repercussions.

Why is Supply Chain Due Diligence Critical for the Energy Sector?

Supply Chain Due Diligence is essential for several reasons, and the stakes are especially high for energy companies.

- **Protection of Human Rights:** The energy sector often involves complex operations in diverse geographies, including regions with lax human rights protections. Supply Chain Due Diligence helps companies in the energy sector identify and address these risks, such as forced labour, child labour, and exploitation.

Real-World Example

The case of [First Solar](#), for instance, demonstrates how lapses in due diligence can lead to severe repercussions. When a third-party audit in Malaysia revealed that migrant workers were subjected to forced labour by subcontractors, it highlighted the risks of modern slavery within the supply chain. This incident shows the need for thorough and continuous supply chain scrutiny and the value of independent social audits in mitigating such risks. First Solar's willingness to be open about the findings promotes transparency and ethical practices and can be seen as a positive step towards corporate responsibility.

- **Environmental Protection:** Beyond compliance, companies in the energy sector have a significant role to play in the drive to net zero and the world's efforts to combat [climate change](#). Supply Chain Due Diligence processes aid the proactive identification and mitigation of environmental impacts outside of an organisation's immediate operations, including emissions, waste management, and natural resource conservation.
- **Responsible Business Conduct:** Due Diligence ensures alignment with ethical business practices, including adherence to international standards. This is critical for energy companies that operate globally and are subject to various regional and international regulations.
- **International Norms:** The energy sector must often align with multiple international norms and standards, making Due Diligence an essential process to harmonise operations and compliance efforts. Initiatives like Solar Energy and [Global Battery Alliance](#) are providing frameworks and guidelines for sustainable and ethical practices in specific energy sub-sectors.
- **Brand and Reputation:** Recent high-profile cases implicating brands in questionable practices have made it even more important for companies in the energy sector to ensure they are not just compliant but are also perceived as responsible corporate citizens.

Real-World Example

Take for example the [Nord Stream 2 pipeline](#), intended to transport natural gas from Russia to Germany, which became a point of international political controversy. Concerns regarding Europe's increasing dependence on Russian energy, coupled with geopolitical tensions, brought the project under scrutiny. Environmental concerns and regulatory challenges added layers of complexity. For companies involved in such international projects, this example underscores the importance of political and environmental due diligence and the potential reputational risks of complex geopolitical relations.

- **Complex Regulatory Landscape:** Energy companies face a myriad of regional and international regulations, including those focused on reducing carbon emissions and ensuring sustainable energy production as well as those relating to social factors such as modern slavery and child labour. Non-compliance is not an option, given the severe penalties, including substantial fines, exclusion from public sector contracts and loss of operating licenses.

What Does Supply Chain Due Diligence Encompass in the Energy Sector?

Supply Chain Due Diligence is a comprehensive process that has been developed to align with internationally recognised human rights and environmental conventions and standards. These include the ILO Fundamental Conventions, OECD Guidelines for Multinational Enterprises, OECD Due Diligence Guidance for Responsible Business Conduct, and UN Guiding Principles on Business and Human Rights. The main intent of supply chain due diligence is to foster responsible business behaviour, mitigating negative impacts on people and the environment, while maintaining economic growth.

For companies in the energy sector, this Due Diligence process takes on additional layers of complexity and urgency. Companies must engage in a robust, risk-based approach to identify and manage a large number of human rights, environmental, and climate-related risks, particularly those that are present within their supply chains. This is crucial for energy companies given the specific challenges they face, such as heightened scrutiny on carbon emissions and resource conservation.

- **Risk Assessment:** Companies in the energy sector should engage in a robust scoping exercise that goes beyond compliance to understand the risks lurking within their supply chain. This could range from labour issues to cyber risks to environmental concerns specific to energy extraction and production.

Real-World Example

The [Fukushima Daiichi Nuclear Disaster](#) underscores the critical importance of risk assessment in energy supply chains. The event highlighted the catastrophic consequences of insufficient due diligence, particularly in the management of nuclear materials and safety protocols. It showed that, even advanced systems can fail, with dire implications for public health, environmental safety, and socio-economic stability.

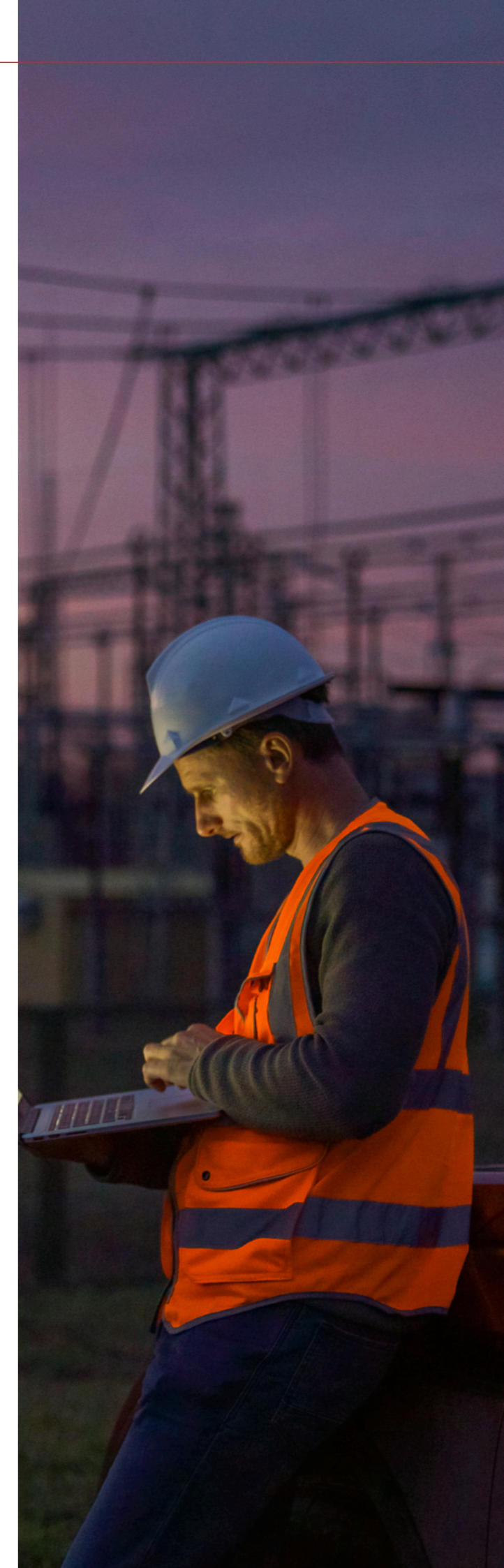
- **Integrating Due Diligence:** The sector is more complex and higher than many other industries for many reasons requiring due diligence measures be integrated into corporate strategies. Energy production, especially in traditional forms like fossil fuels, has substantial environmental consequences, including air and water pollution, greenhouse gas emissions, and habitat destruction. Energy projects often have profound social implications, including land use, community displacement, and impact on local economies. Geopolitical tensions and disruptions often impact the availability and pricing of resources. Incorporating due diligence into corporate strategies enhances transparency and accountability, allows potential ethical and compliance issues to be addressed, helps build trust with stakeholders and investors and contributes to operational efficiency and resilience. This, in turn, can contribute to a positive corporate reputation and attract socially responsible investments. This involves not just compliance teams but also executive leadership to minimise impact on overall business operations and involves continuous monitoring and periodic audits of operations and supplier networks.
 - **Transparency and Reporting:** High levels of transparency are imperative in the energy sector to build trust, compliance, environmental responsibility, and resilience. This includes detailed public reporting, which could be part of sustainability reports or standalone disclosures.
 - **Complaints Mechanism:** Companies should establish robust grievance redressal mechanisms, allowing for anonymous reporting and swift action on any complaints or revelations related to human rights violations or environmental damage.
 - **Technology and Data Analytics:** Leveraging technology for monitoring and predictive analytics can provide a competitive edge, allowing for proactive rather than reactive risk management and enhancing operational efficiency, cost management and resilience.
- The growing recognition of the need for companies to take responsibility for their supply chains is especially pertinent for the energy sector. It reflects a shift in the industry towards ensuring that business practices are not just compliant but are also sustainable and ethical.

Obligations and Responsibilities for Energy Companies

Companies in the energy sector have specific obligations and responsibilities when it comes to Supply Chain Due Diligence due to the unique and impactful nature of their operations. These include:

- **Integration of Due Diligence into Corporate Policies:** Due diligence is a critical tool for identifying and assessing risks associated with various aspects of a company's operations, including financial, legal, operational, and reputational risks. It allows companies to implement effective risk mitigation strategies, minimising the likelihood of adverse events. It also ensures that a company is aware of and complies with all relevant legal and regulatory requirements. For this reason, Due Diligence should be a cornerstone of the corporate governance structure. By integrating these processes into their corporate policies and procedures, companies can enable better-informed, more strategic decisions at every level.
- **Risk Analysis and Mitigation:** Conduct a comprehensive [risk analysis](#) to identify potential adverse impacts within the supply chain. For the energy sector, this is of particular importance as the risks can range from geopolitical instabilities to environmental hazards. Companies should then establish proactive measures to prevent and mitigate these identified adverse impacts.
- **Monitoring and Accountability:** Establish methods for [ongoing monitoring](#) of the effectiveness of Due Diligence procedures, including key performance indicators (KPIs) that align with both regulatory requirements and corporate sustainability goals.
- **Public Communication:** Transparency is becoming increasingly important in the global energy sector, given increasing levels of public and regulatory scrutiny and high profile incidents. This may involve publishing a detailed report or integrating Due Diligence information into existing sustainability reports.
- **Director Responsibilities:** In accordance with emerging legislation like the EU's Corporate Sustainability Due Diligence Directive (EU CS DDD), directors are not just responsible for financial performance but also for overseeing the implementation of robust Due Diligence processes.
- **Reputational Consequences:** While non-compliance can result in legal penalties such as fines and trade sanctions, the reputational damage can be far more devastating and long-lasting. Given the spotlight on 'greenwashing' and ethical practices, failing to comply can erode trust and brand value at an exponential rate, which can be far more detrimental than any immediate legal repercussions.

By focusing on these obligations and responsibilities, energy companies not only align with international laws but also position themselves as ethical and sustainable players. This can offer a competitive edge in a marketplace that is increasingly valuing transparency and ethical conduct over mere compliance.



What are the Benefits of Compliance?

Taking a proactive approach to Supply Chain Due Diligence and sustainability brings immense advantages, particularly for energy companies navigating complex regulatory and stakeholder landscapes. Here's how:

- **Improved Reputation:** The energy sector often finds itself under scrutiny for environmental and social issues. A proactive approach to Supply Chain Due Diligence helps in building an organisation's reputation as responsible and ethical, key factors in gaining the trust of stakeholders and customers. Moreover, it serves as a shield against accusations of 'greenwashing,' enhancing your credibility in a sector that's increasingly sensitive to such issues.
- **Reduced Risk:** Compliance is especially important for the energy sector, given the inherent risks like cyber vulnerabilities, geopolitical instabilities, and complex supply chain networks. A well-executed Due Diligence process reduces the risk of legal repercussions, fines, and, most crucially, the often-irreparable reputational damage. It also ensures you're prepared for sudden shifts in regional or industry-specific regulations, a common occurrence in the energy sector.
- **Increased Efficiency:** The energy sector often involves complex, global supply chains. Having a clear understanding of your supply chain and your supply chain risks enable more efficient supply chain management including more streamlined operations, cost optimisation, and even more responsible resource allocation, which is an important part of achieving long-term sustainability.
- **Competitive Advantage:** As the energy sector transitions to greener alternatives, a strong ESG compliance record can provide a significant competitive edge. It's not just about attracting customers, but also positioning your company as a leader in responsible energy production and supply chain management. This can also make your company more attractive to investors who are increasingly looking at [ESG performance as a key indicator](#).
- **Long-Term Sustainability:** For energy companies, sustainability isn't just a buzzword; it's a long-term business imperative. By adhering to stringent Due Diligence measures, you're not just avoiding risks—you're also building a more resilient, sustainable business with significant improvement in operational efficiencies, which can lead to an improved bottom line. This approach will resonate with consumers and investors leading to increased market share, as well as positively impacting the well-being of employees and the broader communities impacted by your supply chain, often located in geopolitically sensitive regions.

How to Get Started on the Path to Supply Chain Due Diligence in the Energy Sector

Embarking on a Supply Chain Due Diligence journey can be intricate, especially for energy companies dealing with complex, often global, supply chains and rapidly evolving regulations. Here's a roadmap to start:

- **Develop a Due Diligence Policy:** The first step is to formulate a policy that delineates the procedures and actions your energy company will undertake to mitigate supply chain risks. Align this policy with international frameworks such as those published by the OECD and ILO and regulations such as the forthcoming [EU Corporate Sustainability Due Diligence Directive](#), the USA's [Uyghur Forced Labor Prevention Act](#), and other relevant regional and sector-specific laws. Get executive endorsement before cascading this policy to all stakeholders involved to demonstrate your organisational commitment.
- **Assess Your Supply Chain:** Understanding your supply chain is key, particularly in the energy sector where raw materials can come from geopolitically sensitive areas. Identify all suppliers, subcontractors, and other business partners and evaluate their compliance with international and energy-specific standards.
- **Implement Due Diligence Measures:** Actions speak louder than policies. Implement concrete measures like risk assessments, audits, and supplier engagement programs. Given the sector's specificity, consider additional checks for energy-related compliance, such as carbon footprint assessments and compliance with renewable energy mandates.
- **Monitor and Evaluate Performance:** Continual monitoring is key, especially in a sector where regulations and

technologies are constantly evolving. Utilise KPIs that are pertinent to the energy sector, such as emissions reduction, to evaluate the effectiveness of your Due Diligence measures. This process should be ongoing and aimed at continual improvement within the supply chain.

- **Publish Performance Reports:** Transparency is essential. Publish comprehensive reports that not only fulfil legal obligations but also provide insights into your due diligence process. Given the energy sector's spotlight position in sustainability debates, these reports can serve as a tool in brand and reputation management and help build stakeholder trust.
- **Engage with Stakeholders:** In the energy sector, this goes beyond the usual suspects to include regulatory bodies, environmental organisations, and even local communities affected by your operations. Their input can provide valuable insights into how your due diligence efforts are perceived and where they might be improved.
- **Seek External Support:** Given the complex nature of energy supply chains and the severity of associated risks, external expertise can be invaluable. Whether it's legal advice on complying with new regulations or technological solutions for better supply chain visibility, don't hesitate to seek outside help.

In summary, a comprehensive and sector-specific approach to Supply Chain Due Diligence is vital for energy companies. It goes beyond ticking regulatory boxes; it's about proactive risk management, brand protection, and long-term sustainability in a sector that's under increasing scrutiny.



Challenges of Effective Supply Chain Due Diligence in the Energy Sector



Implementing Supply Chain Due Diligence is far from a straightforward task, and companies, particularly in the energy sector, encounter a number of challenges. These challenges often parallel those seen across a wide range of organisations but are heightened due to the energy sector's inherent complexities and regulatory scrutiny. Here's a deep dive:

- **Supply Chain Complexity:** Energy companies often deal with multi-tiered, global supply chains involving raw materials like rare earth metals, crude oil, and natural gas. The complexity is even more pronounced when these resources come from geopolitically sensitive or hard-to-access regions.
- **Data Collection:** The energy sector requires specialised data, often exceeding standard operational metrics. This data, from carbon emissions to human rights adherence, can be in multiple formats, exacerbating the challenges of effective data collection and systematization.
- **Veracity of Data:** Given the sector's highly regulated nature, the stakes for data accuracy are exceptionally high. Companies may be tempted to use AI-generated or web-scraped data to save money or for expediency, but such sources often lack the rigorous verification needed for regulatory compliance and stakeholder trust.
- **Lack of Transparency:** This is a critical issue, especially when dealing with suppliers in countries where regulations are lax or non-existent. The opacity can make it very difficult to assess and mitigate risks effectively.
- **Limited Capacity:** Both buyers and suppliers in the energy sector may lack

the capacity to manage these complex data streams. For smaller energy companies or suppliers, the resource limitations can be a significant barrier to effective due diligence.

- **Cost of Compliance:** This is particularly burdensome for SMEs in the energy sector, where the costs related to due diligence processes, supplier audits, and risk mitigation can quickly escalate.
- **Knowing What is Enough:** Regulatory requirements in the energy sector are continually evolving, making it challenging to know what suffices for compliance. For more insights, refer to our blog: [“When is enough, enough?”](#)
- **Legal Liability:** The legal risks for non-compliance are significant and can result in not just fines but also far-reaching reputational damage, given the energy sector's public scrutiny.
- **Coordination with Suppliers:** Supplier collaboration is pivotal for a transparent and effective due diligence process. Cultural and legal discrepancies, especially in an international context, can further complicate this engagement.
- **Time Constraints:** Regulatory mandates often come with strict timelines for implementation. Given the extensive nature of energy supply chains, adhering to these timelines can be a daunting task, with legal repercussions for lapses.

Navigating these challenges requires a robust, sector-specific strategy that not only addresses these issues but also anticipates future complexities, particularly as the energy transition accelerates.

Conclusion

The landscape of Supply Chain Due Diligence is complex, and the stakes are especially high in the energy sector. However, the cost of non-compliance can be far greater than just legal repercussions; it can significantly harm a company's reputation. While the journey toward comprehensive due diligence and sustainability may be fraught with challenges, the benefits of improved risk management, operational efficiency, and stakeholder engagement are undeniable.

Companies must adopt a comprehensive, risk-based approach that goes beyond mere compliance. This involves not only implementing stringent due diligence measures but also continually refining these processes in response to evolving risks and regulations. Given the sector-specific challenges, companies should consider seeking external expertise to ensure that their due diligence processes are both robust and compliant.



About Achilles

For over 30 years, Achilles has protected organisations' business interests and reputations by providing unrivalled levels of supply chain transparency, carbon reduction and management. We are the ESG and carbon management partner of choice for the world's leading global brands.

Achilles specialises in supporting customers that require truly robust environmental, social and governance reporting to fully comply with ESG regulation, meet investor requirements and achieve their own ambitious sustainability goals. We work with market-leading financial, industrial, commercial and governmental organisations requiring the serious, detailed analysis and expert insight necessary to deliver exceptional reporting confidence and positive social and environmental impact.

Operating from 17 locations worldwide, Achilles is at the forefront of the battle against climate change, a champion for social justice and human rights, and an expert in health, safety, and risk management.

How Achilles Elevates Your Supply Chain Due Diligence

Achilles functions as an extension of organisations needing all-encompassing supply chain due diligence solutions and in-depth data insights vital for international legislative compliance. But we go beyond compliance; our sustainability services and supplier development programs are geared to improve your supply chain performance.

Our Services Include:

- **Supply Chain Evaluation:** Our comprehensive data collection covers supplier documentation, publicly available and historical online information, and investigative reports from NGOs and charities. Notably, our Transparency questionnaire incorporates insights from our extensive global audit program and firsthand accounts from workers in relevant industries and regions, offering you a thorough view of your supply chain risks.
- **Risk Assessment:** Our detailed supply chain evaluation facilitates a broad scoping exercise to uncover hidden

risks within your supply chain. This multi-disciplinary approach is essential for effective due diligence and for demonstrating to authorities that you've adequately mitigated these risks.

- **Due Diligence:** Our audit teams, strategically located globally, conduct thousands of desktop and on-site audits annually. They scrutinise documentation, physically inspect workplaces, and confidentially interview individuals who might be subjected to unethical employment practices or human rights violations.
- **Remediation and Reporting:** We are committed to the ongoing improvement of global supply chains. Our tracking of audit findings and remedial actions, backed by our team of data scientists, provides you with comprehensive supply chain data suitable for inclusion in annual reports.

To discover how Achilles can assist you in meeting your supply chain due diligence requirements, feel free to [contact us](#).





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