Löning *Human Rights & Responsible Business*

German Supply Chain Due Diligence Law

– Content and significance –

Briefing paper

Why is there a Supply Chain Due Diligence Law?[1]

International trade and business operations by German and European companies represent an opportunity to create jobs and generate prosperity along global supply chains. On the downside, these activities can also have substantial negative effects on the people and the environment along those same supply chains. In addition to the duty of the state to respect, protect and fulfil human rights, companies also have the responsibility to respect human rights. In order to ensure the practical implementation of this responsibility as well as to create clear rules and the same conditions for all companies in Germany, the German Federal Cabinet adopted the Supply Chain Due Diligence Law.

The Law was passed by the German Parliament (Bundestag) and Federal Council (Bundesrat) in June and is planned to come into force in January 2023. Beyond this Law, your company may also be subject to EU and other legislation requiring the implementation of human rights due diligence. Our team is happy to support you by providing a practical overview of all national and EU legislation relevant to your company.

1 Disclaimer: the contents of this briefing paper do not constitute legal advice and are provided for general and practical information purposes only.

What does due diligence mean?

The Law requires companies operating in Germany with a certain number of employees to take the necessary steps to prevent, end or minimise adverse impacts on people and the environment. In practice, this means that companies need to set up a management system to identify if and where their business activities could potentially cause or contribute to human rights abuses or environmental damage. The Law specifies which elements such a management system must include.

Responsibility to minimise adverse impacts on people and the environment

The due diligence requirement is not an *obligation to succeed* as companies are not able to guarantee that no human rights or environmental obligations have been violated in their supply chains. Instead, companies will have to prove that they follow the due diligence obligations as set out in the Law to the best of their ability, considering their individual context and the appropriateness of their actions. The appropriateness as set out by the Law is defined by considering, among other things, the type and scope of the business activity, the severity of the violation and the company's ability to influence it. We have successfully been working with companies for many years in order to define this individually for each company.

Who does the Supply Chain Due Diligence Law apply to?

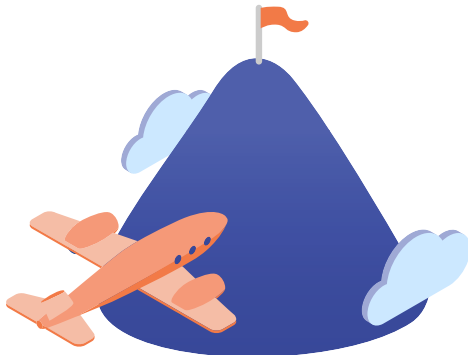
The Supply Chain Due Diligence Law applies to all companies that have their head office, registered office or a branch office in Germany. Initially, this applies to businesses with more than 3,000 employees and after 1st of January 2024, it will apply to businesses with more than 1,000 employees.

Businesses with more than 3,000 employees and 1,000 employees as of 2024

All temporary employees as well as employees of all affiliated companies have to be taken into account in this calculation. Additionally, the effects of the law are also expected to impact smaller companies, as requirements will be passed on in the supply chain.

The supply chain refers to all products and services of a company (from raw material to finished product) and includes:

- the actions of a company in its own area of business (including controlled subsidiaries abroad),
- the actions of a direct supplier, and
- the actions of other indirect suppliers. (§ 2 (5))



Core requirements for companies:

According to the Supply Chain Due Diligence Law, companies are required to set up a management system to fulfil their due diligence obligations. This management system must ensure that human rights and environmental risks are identified, and any potential violations are prevented, ended, or minimised (§ 4).

It must include the following:

1.

Establish an appropriate and effective risk management system which is anchored in all relevant business activities through respective measures.

2.

In practice, this risk management must include the following measures:

- Delegating in-house responsibility (§ 4 (3)) for the topic of human rights and the risk management system, for example, by appointing a human rights officer.

- Conducting regular risk analyses (§ 5) to identify human rights or environmental risks in the company (including its own operations) and at direct suppliers. The risk analyses should be conducted annually and whenever necessary (e.g., when expanding business activities, dealing with new suppliers or when new evidence arises).

Human rights are those arising from the conventions listed in number 1 to 11 of the Annex to the Act (§2 (1))

A human rights risk is a condition in which, on the basis of factual circumstances, there is sufficient likelihood of a violation of one of the following prohibitions for the protection of the human rights listed in the convention (of the Annex):

- child labour
- forced labour
- all forms of slavery
- disregarding occupational health and safety
- disregarding freedom of association
- unequal treatment
- withholding reasonable wages
- causing environmental damage (harmful soil change, water and air pollution, harmful noise emission and excessive water consumption) and impairing food safety, access to drinking water and sanitary facilities or a person's health
- unlawful eviction and deprivation of land
- hiring security forces, which make abusive use of the force
- any other prohibition of an act or omission in breach of duty, directly capable of infringing in a serious manner the human rights set out in §2. 1

3.

Formulating a policy statement (§ 6 (2)) on the respect for human rights and the environment which is adopted and endorsed at the highest management level. The policy has to contain a description of the implemented due diligence management system, the main human rights and environmental risks identified through the risk analyses and a clear formulation of expectations towards employees and suppliers (e.g., through a code of conduct).

4.

Adopting concrete measures to prevent violations of human rights and environmental provisions for the company's own business activities as well as for direct suppliers (§ 6 (1 - 4)). The effectiveness of the measures shall be assessed annually and on an ad hoc basis.

- Measures **in own business areas** include among others delivering employee trainings, adapting procurement strategies and buying practices as well as implementing control measures.

- Measures **for direct suppliers** can encompass, for instance, the selection of suppliers according to human rights and environmental considerations, contractual assurance by a direct supplier to comply with the expectations, implement risk-based control mechanisms (such as audits) or trainings on the measures.

5.

Should any human rights or environmental provision be violated by the company or a direct supplier, remedial actions must be taken. The effectiveness of these remedial actions shall be assessed annually and on an ad hoc basis (§ 7 (1 - 4)).

- In case a violation has occurred or is imminent, the company has to **prevent, end or minimise** the violation. **If the violation is in its own business area,** the company must ensure that the **remedial action ends the violation.**
- In the case of **direct supplier** and if the company cannot end the violation, a concrete plan of **actions to minimise the violation** should swiftly be implemented. Termination of the business relationship shall only be considered as a last resort.

6.

When violations or imminent risks are identified, the responsible person in the company must be informed quickly. The Law thus requires companies to establish internal complaints procedures (§ 8), also known as grievance mechanisms. The effectiveness of the procedures shall be assessed annually and on an *ad hoc* basis.

- The complaints procedures are meant for persons who are directly affected either by the economic **activities in the company's own business area** or by economic **activities of a direct supplier** or for persons who are aware of a possible violation they would like to submit.
- The procedures have to fulfil certain criteria, such as (but not limited to) being impartial and confidential, and ensuring that the complainant is protected from disadvantage or punishment.
- Companies can participate in external mechanisms instead if these fulfil all criteria.

7.

The above-mentioned complaints procedure must also be open to persons who have knowledge of possible violations or whose rights have been affected by economic activities of an indirect supplier (§ 9 (1)).

If the company has *substantiated knowledge* of possible violations (e.g., through the complaints procedures, its own findings, responsible public authorities, human rights reports or other sources), it shall immediately conduct a risk analysis, establish appropriate preventative measures (such as the implementation of sector initiatives); create and implement a concept to the prevent, end or minimise the violation and update the policy statement, if necessary.

Environmental obligations are those arising from the conventions listed in number 12 and 13 of the Annex (§2 (3))

Environmental risk is a condition in which, on the basis of factual circumstances, there is reasonable likelihood of a violation of one of the following prohibitions arising from the environmental duties listed in §2 (3):

- The ban on the manufacture, the use and treatment of mercury pursuant to the Minamata Convention
- Prohibition on the production and use of chemicals and the non-environmentally sound handling, collection, storage and disposal of waste arising from the Stockholm Convention
- The control of transboundary movements of hazardous wastes as defined by the Basel Convention

8.

The due diligence activities shall be continuously documented within the company (§ 10), including all responsibilities, processes and measures mentioned above, as well as any identified violations. Such documentation serves as evidence for the company that its due diligence was appropriate and effective and is required to be retained for seven years. The company also has to submit and publish on its website an annual report on the fulfilment of its due diligence obligations, covering, for example, the human rights and environmental risks identified and the effectiveness of implemented measures.

Should companies subject to the Law fail to appropriately fulfil their due diligence obligations, the federal authority responsible for the enforcement of the Law is authorised to issue substantial fines. Any additional civil liability is explicitly excluded (§ 3 (3)).

How can we support you?

We are an international management consultancy specialised in human rights. With our multinational and interdisciplinary team of experts, we help companies establish and integrate effective human rights due diligence processes such as specified by the Law, for example by identifying:

1. where your most important risks are (Risk analysis),

2. what processes you have already embedded in your company (Gap assessment),

3. what your next steps should be (Roadmap).

We also offer a practical overview of all relevant national and EU regulation to help you understand the requirements your company is subject to.

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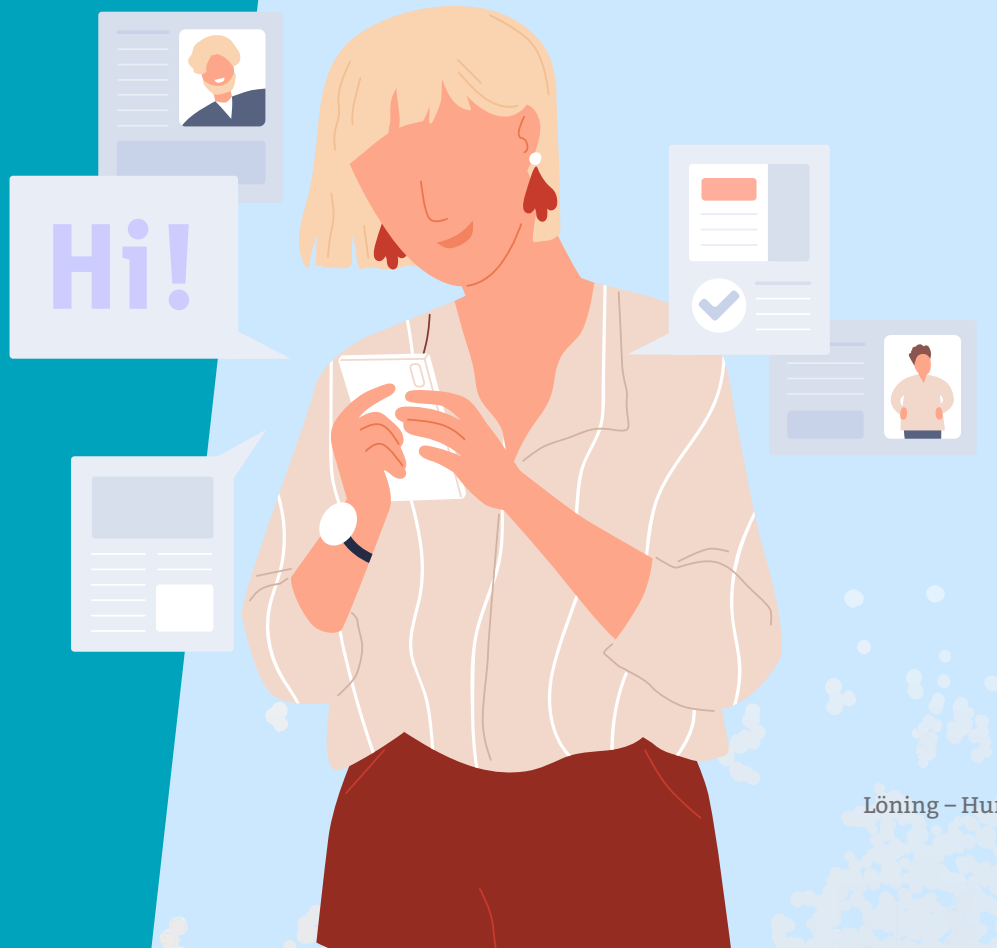

We are happy to answer any questions you may have in relation to your obligations under the Supply Chain Due Diligence Law.

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