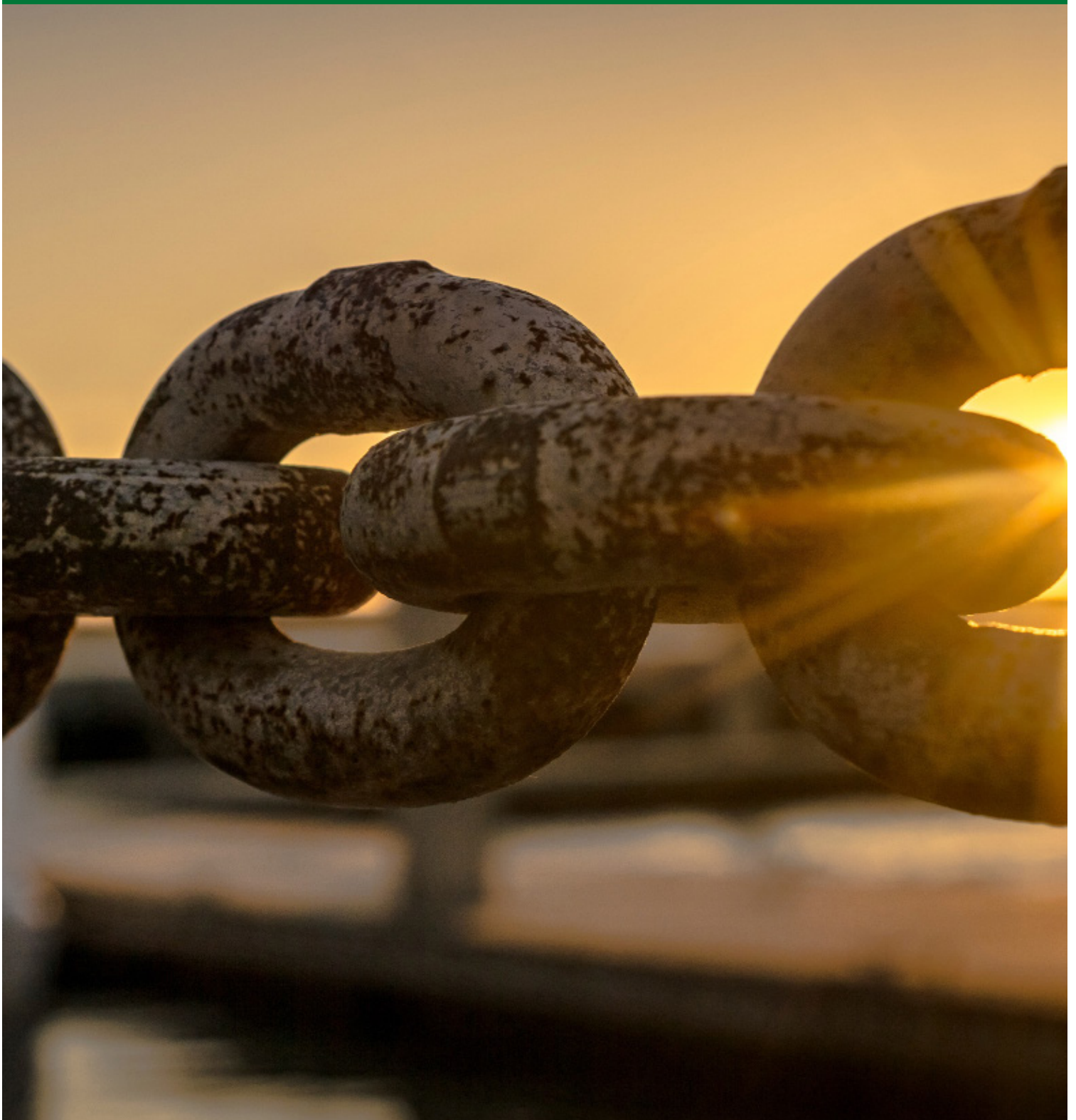


Guide to the German Supply Chain Due Diligence Act



On 11 June 2021 the Supply Chain Due Diligence Act (the "Act") passed the German Federal Parliament, on 25 June 2021 it passed the German Federal Council. It will come into force on 1 January 2023 (applicable to German companies of at least 3,000 employees; as of 1 January 2024 of at least 1,000 employees). In legal terms, the Act primarily means that companies will need to adapt and update their compliance and sustainable contract drafting, particularly when it comes to purchasing.

This guide makes recommendations in line with the legal duty of care catalogue (= risk management, risk analysis, policy statement, preventive measures, remedial measures, complaints procedure and documentation and reporting obligations), so that companies can comply with the legal requirements.

For an overview on which companies are affected by the law, what the law requires and what sanctions may be imposed for violations, [click here](#).

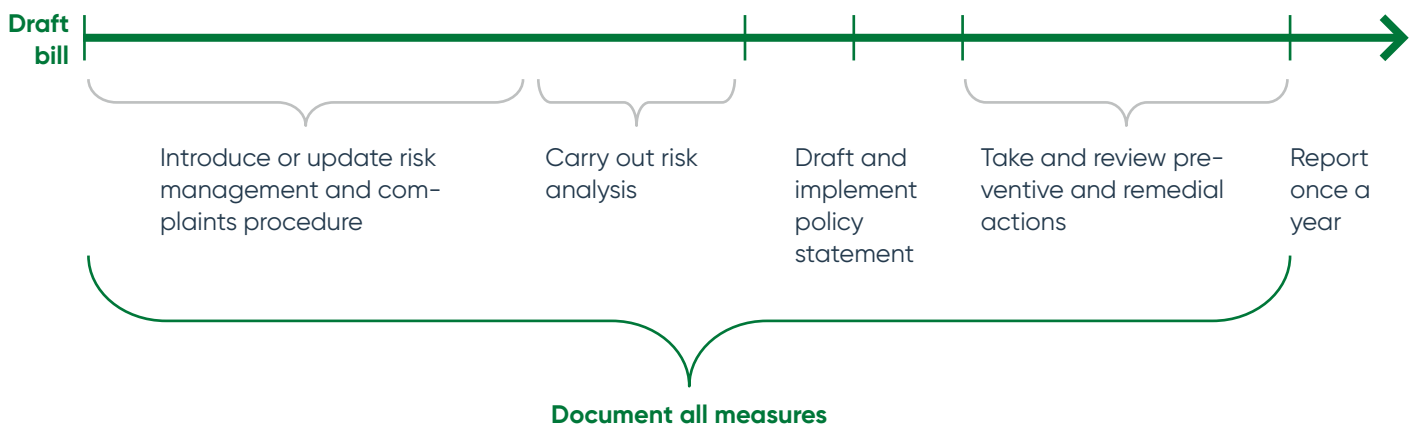
What needs to be done specifically?

1 „To-do“
Introduce or update risk management and conduct risk analysis as well as establish complaints procedure/document all these measures.

2 „To-do“
Draft or revise policy statement.

3 „To-do“
Take or review preventive and remedial actions where risks are identified, e.g. supplier selection/control, codes of conduct, training, sustainable contract design/document all these actions.

4 „To-do“
Report once a year.



1 Risk management

The Act requires companies to introduce and effectively implement adequate risk management. Here is what you should do:

- Set up a „**Supply Chain Act Roundtable**“ to allocate and define long-term responsibilities. At a minimum, the management, compliance, legal, purchasing and (if available) CSR department should be involved. **Tip:** Other departments may also be able to contribute valuable information, e.g. product development, quality management. The „Supply Chain Law Roundtable“ should meet on a regular basis.
- Track the **responsibilities/monitoring measures** in writing (in your compliance management system). **Tip:** If you already have a company-wide CSR/sustainability strategy, it makes sense to integrate your measures for the implementation of the Act into this strategy (see, for example, provision 6.6.6 of the ISO 26000).
- As the management, define the **financial and human resources** for appropriate monitoring of the supply chain (= own business as well as direct supplier, in case of substantiated knowledge, also indirect suppliers). A study by the EU Commission estimates additional costs of 0.005% of turnover for monitoring the entire supply chain.
- The Act recommends the creation of the **position of a human rights officer** reporting directly to the management. **Note:** When creating a new position, care should be taken to ensure that this person is sufficiently informed and involved in a timely manner to fulfil his/her duties. He / she should be in regular exchange with other departments involved in order to avoid system errors and minimise human error.
- At least once a year and on an occasion-related basis, the **management must be informed about the current status of the work.**

2 Risk analysis

The Act requires companies to conduct an appropriate risk analysis as part of the risk management. Here you should do the following:

- At least once a year and on an occasion-related basis: **Determine whether there is a risk that your own business actions or business actions of your direct (or indirect in the case of indications) supplier violate human rights.** A risk analysis is „occasion-related“ if the company must expect a significantly changed or significantly expanded risk situation in the supply chain, for example due to the introduction of new products, projects or a new business field. **Tip:** Anchor the principle of regular risk assessment in your compliance management system.

- To do this, **take stock of all of your company's business activities and business relationships** → Where could human rights be affected? These arise from internationally recognised agreements, in particular the ILO core labour standards, which are referred to exhaustively in the Act. **Note:** The risks for potentially affected persons are to be identified, not the risks for the company itself.
- **What is the best way to take stock?** According to the Act, the method of gathering information is at the discretion of the company. **Tip: Use internal knowledge and existing mechanisms first.** As described above under risk management, a Supply Chain Act Roundtable makes sense here. **Also access external knowledge**, such as the „*Infoportal Menschenrechtliche Sorgfalt*“ of the German UN Global Compact or CSR Risk Checks online (e.g. <https://www.mvorisicochecker.nl/en>). **Further approaches may be useful or even necessary**, e.g. conduct supplier interviews (especially if the supplier might have superior knowledge or the risk originates from its sphere), conduct on-site inspections, seek discussions with (potentially affected) stakeholders, such as workers, trade unions, local residents. Also take into account findings from the processing of tips gathered in the complaints procedure. **Compliance tip:** Possible contents for interviews/inspections as well as the associated responsibilities, process flows and control mechanisms should be collected and recorded in advance.
- **Present the results in a risk map:** e.g. according to business areas, locations, products, countries of origin.
- **Prioritise the identified risks** (according to „appropriateness criteria“ = (i) the nature and scope of the business, (ii) the company's ability to influence the immediate violator, (iii) the expected severity of the violation, (iv) the reversibility of the violation, (v) the likelihood of the violation occurring, (vi) the nature of the contribution to causation), especially if you cannot address everything at the same time. **Note:** Prioritisation is also not about the company's interests, but the interests of the (potentially) affected parties. **Tip:** In the Act, under the criterion of ability of influence, the „*procured quantity*“ is mentioned as an example. You should take this into account in contractual provisions.
- **Communicate the results of the risk analysis to the relevant decision-makers in the company**, in particular management, legal, compliance, purchasing, CSR department, human rights officer(s).

3

Policy statement on procedures, risks, expectations of employees and suppliers

The Act requires companies to adopt a policy statement and sets out the minimum content in doing so. Here is what you should do:

- As the management, adopt a policy statement that must include: (i) a description of the company's **duty of care process**, (ii) the **risks identified in the risk analysis** with reference to the relevant international agreements, (iii) **the company's human rights and environmental expectations of its employees and suppliers**.
- **Note:** Policy statements are regularly brief and only broadly state that the company is committed to protecting human rights, which risks in particular the company has identified and what it is doing and expects to do about them (human rights strategy). There are numerous templates on the internet that you can use as a basis. The policy statement serves as the basis for your own code of conduct and the supplier code of conduct. **Tip:** Check (also in the future) whether your existing policy statement is specific enough, as the Act requires that the company at least specifies its essential measures in the context of risk analysis, prevention, remediation, reporting obligations and complaints mechanism. The human rights-related expectations are likely to regularly lie in mitigating and averting human rights risks.
- **Communicate the (new) policy statement** to workers, the works council, suppliers in the supply chain and the general public.

4

Take preventive measures in your own business

The Act requires companies to immediately establish appropriate preventive measures in its own business if a risk is identified. Here you should do the following:

- Develop / update your **codes of conduct for your own business, based on the policy statement. Make regular updates.**
- Integrate **sustainability into your purchasing practices.** Purchasing has a crucial role in avoiding and minimising human rights risks. **Tip:** For guidance on what sustainable procurement can look like, see ISO 20400 *"Sustainable Procurement"* where you find information on strategy, organisation and processes. **Note:** Interestingly, the explanation of the Act specifically mentions **contract design elements** that have a significant influence on the human rights risk, e. g. purchase prices, delivery times, cost specifications, time pressure. Therefore, especially when concluding contracts in high-risk areas, make sure that the overall design of the contract does not increase the risk of human rights violations. In addition to the relevant contractual elements mentioned in the draft, other elements such as payment terms (not too long) should be taken in to consideration. Moreover, it is advisable to offer the supplier incentives such as bonus regulations or an extension of the business relationship/contract extension option if certain sustainability goals are achieved, or participation in sustainability investments. On the topic of "sustainable contract drafting", also read our publication *"Sustainable Supply Chains"*.
- **Procurement guideline:** For individual procurement steps (e. g. product development, order placement, purchasing, production lead times), determine which precautions are to be taken to minimise or prevent the identified risks.
- Conduct **employee training/education on the relevant codes of conduct and guidelines** (especially in purchasing), e. g. during on-boarding of new employees. **Tip:** Regular training courses lead to a corresponding sensitisation of the employees and reduce resistance (trade-off thinking). This increases the chances that the implementation measures under the Act will not fail due to a lack of change management. **Compliance tip:** As far as possible, expand your existing training to include the topic of the Act.
- **Check on a risk basis** whether the defined measures are actually adhered to and implemented in the individual business areas in the company.
- The **effectiveness** of the **preventive measures** mentioned under "4" **must be checked once a year as well as on an occasion-related basis.** Findings from the processing of information given in the complaints mechanism shall be taken into account. The measures must be updated immediately if necessary. **Tip:** In order to be able to evaluate whether individual measures are effective, it makes sense to set concrete goals, e. g. with regard to the number of training sessions.

5 Preventive measures with regard to suppliers

The Act requires that companies must immediately establish appropriate preventive measures with regard to a supplier if a risk is identified. Here you should do the following:

- **Make careful supplier selection and supplier assessment.** **Note:** Certifications such as SMETA (SEDEX), SA8000, BSCI or industry-specific seals are only an initial guide, as their content varies. In certain supply chains, there may not even be any suppliers who already have a certificate; in this case, it is even more important that any careful supplier selection also requires your own interviews and checks against your own human rights- and environment-related expectations. **Compliance tip:** Link human rights and environmental issues to existing processes when assessing your business partners.
- Develop/update your **supplier code of conduct** based on the policy statement. **Make regular updates.** Attention to supplier development (e.g. long-term cooperation) can also be useful, especially in identified problem areas. Participation in industry initiatives can also be useful and have a risk-minimising effect; in addition, it can possibly increase influence and achieve synergy effects.
- **Drafting contracts: Commit your contractual partner properly.** In addition to general codes of conduct, this also requires specific provisions in individual contracts, depending on the results of the risk analysis. Contractual regulations consist of an interplay between obligations (conduct obligations, reporting obligations, auditing obligations) and sanctions such as contractual penalties and termination options. The Act also mentions further examples, such as that the contractual partner must only purchase products from selected (previously audited) suppliers or must provide proof that certain products come from certified regions or raw materials from certified smelting plants (chain of custody certification). Interestingly, the Act also specifically mentions the use of “pass-on clauses” in relation to upstream suppliers. In other words, the supplier is to be obliged to enforce its supplier code of conduct also vis-à-vis its suppliers by means of suitable contractual provisions. **Note:** Until now, such “pass-on clauses” have been viewed critically under German law on GTC’s, as they can restrict the supplier’s freedom of disposition, so that “effort clauses” have so far tended to be considered permissible. This could change as a result of this law and lead to a need to edit corresponding provisions in supplier code of conducts. On the topic of “sustainable contract drafting”, please also read our publication „Sustainable Supply Chains”.
- Conduct **supplier monitoring**, especially **with regular audits of suppliers.** **Compliance tip:** Specify in particular which types of checks are to take place (self-disclosure, self-audit, external audit, audit with certification), which questions are to be asked of the supplier, how often such checks are to take place, how this process is to be checked internally and thus designed to be audit-proof.
- Conduct **supplier training/education** on your expectations and identified risks.
- The effectiveness of the preventive measures mentioned under “5” **is to be reviewed once a year as well as on an occasion-related basis.** Findings from the processing of notices according to the complaints mechanism are to be taken into account. The measures must be updated immediately if necessary. **Tip:** In order to be able to measure whether individual measures are effective, it makes sense to set concrete targets, e.g. with regard to the number of “sustainably” selected suppliers or the number of reviews.

6

Remedial measures

The Act requires companies to take immediate remedial action to prevent, end or minimise imminent or actual violations. Here is what you should do:

- In **your own business**, you must take **remedial action** leading to the **cessation of the violation**.
- In the case of (imminent) violations in the **business of your direct (in case you have “substantiated knowledge” also your indirect) supplier**, if you are not in a position to stop the violation yourself, you must immediately prepare, together with the supplier, a **corrective action (time) plan** to minimise and prevent the violation, typically including the following elements: (i) First, ask your supplier to correct the non-compliance by a specific date. Make your requirements clear and offer concrete support. For example, consider involving affected people, trade union representatives or civil society organisations. (ii) Join forces with other companies to increase pressure on the supplier (e.g. through industry initiatives or through other companies working with the supplier). (iii) If it is foreseeable that the supplier will not comply, enforce a penalty, temporarily suspend business relations or remove the company from possible award lists until the supplier stops the violation. **Compliance tip:** Regularly check whether your escalation levels are leading to success and define responsibilities, both in terms of who has which tasks internally and who is to be informed in which cases. Document your measures. **Tip:** So far, the Act requirements for an action plan will often not be included in a code of conduct in this form, so contractual adjustments should be considered.
- **Breaking off business relations with a supplier** is only envisaged **as a last resort** in the Act. **Tip:** Look at how the topic of „violations“ is reflected in your current codes of conduct. Companies often stipulate that the termination of the cooperation takes place immediately upon the occurrence of a violation. Corresponding regulations may need to be revised.
- The **effectiveness** of the preventive measures mentioned under „6“ **must be reviewed once a year and on an occasion-related basis**. Findings from the processing of reports according to the complaints mechanism shall be taken into account. The measures shall be updated immediately if necessary.

7

Complaints procedure

The Act requires that companies immediately set up an internal complaints procedure. Here you should do the following:

- The complaints procedure serves to enable **(i) (potentially) affected persons** in their own business and in and around the supply chain and **(ii) persons who have knowledge of possible violations to point out human rights and environmental risks and violations**. **Alternatively:** Participation in an external complaints mechanism (e.g. an industry association), provided that it meets the requirements of accessibility, transparency and accountability set out in the law. **Note:** The complaints procedure must therefore be accessible beyond the immediate supplier to the named persons throughout the supply chain.
- **Requirements of complaints mechanism:** The procedure must be set out in writing, in particular: Who are the target groups? What happens when a complaint is made? What procedural steps follow? What is the time schedule? Users do not suffer any disadvantages by using the complaints procedure! Confidentiality and data protection are guaranteed! The persons entrusted by the company with the enforcement of the proceedings must ensure impartiality.

- **Ensure access to and use of the complaints mechanism.** When making it accessible, **a combination of different complaint channels** (depending on the target group) is recommended. For example, consider setting up hotlines/e-mail addresses/websites, complaint forms, labels on products, (internal/external) contact persons. **Note:** Where risks have been identified, special attention should be paid to minimising barriers to the complaints process (e.g. language, fear of consequences).
- To ensure that people are aware of the respective complaint channels, you must provide **public (website) and regular targeted information about the complaints procedure.** The procedure must also be made transparent.
- The effectiveness of the complaints procedure must be reviewed at least once a year or on an occasion-related basis and updated immediately if necessary.
- Difference to **whistleblowing system according to Whistleblowing Directive/Whistleblower Protection Act:** The complaints procedure under the Supply Chain Act is more far-reaching in that it must also be accessible to persons outside the own company. The whistleblowing system according to the Whistleblower Protection Act is broader in its scope of application (reporting of violations of EU law) and provides even more specific requirements on how the whistleblowing system is to be designed. It makes sense to combine measures that will be necessary under both Acts. We are happy to provide support, also in the implementation of technical solutions.

8 Documentation and reporting

The Act requires that companies document the fulfilment of duty of care obligations and report on it once a year. Here you should do the following:

- **Track** your duty of care obligations fulfilled from steps 1 to 7 **on an ongoing basis** and keep the documentation for at least 7 years.
- **Report once a year** (no later than 4 months after the end of the business year) on the previous year's fulfilment of your duty of care obligations, in particular on the risks identified and the measures taken. In addition, assess the effectiveness of the measures and your conclusions for the future. If you have not identified any risks, further explanations are not necessary. Company and business secrets do not have to be disclosed. The Federal Office for Economic Affairs and Export Control (BAFA) provides electronic access for the reporting format.
- Make your **report publicly accessible on your website free of charge** for a period of 7 years.