

Germany's Supply Chain Due Diligence Act

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In June, the German legislature passed the Supply Chain Due Diligence Act ("SCDDA"; in German: Lieferkettensorgfaltspflichtengesetz – LkSG). It will come into force on 1 January 2023. That leaves limited time for in-scope companies to prepare for the new due diligence obligations.

To which companies does the SCDDA apply? Companies with their central administration, principal place of business, administrative headquarters, statutory seat or branch office in Germany and with at least 3,000 employees in Germany must comply with the law. This threshold will be lowered to 1,000 employees as of 1 January 2024. In a group of companies, each company must be examined separately to determine whether the SCDDA applies to it. For the parent company, the employees of group companies must be added to its own employees. The due diligence obligations cannot be delegated to another company, e.g., to the parent company or a subsidiary. Companies to which the SCDDA does not apply must nevertheless get prepared – since the parent company or customers may demand compliance with the SCDDA.

Which due diligence obligations must in-scope companies fulfill? The companies must endeavor to prevent or minimize risks for, and to put an end to violations of, certain human rights and environmental risks in their own area of business and in their supply chains. For this purpose, they must in particular establish a risk management system and conduct regular and ad hoc risk analyses. This applies to their own business area and to direct suppliers (their contractual partners). In the case of indirect suppliers, the company must only start analyzing the risk if there are sufficient indications of a possible violation of a human rights-related or environment-related obligation. If the company identifies a risk, it must take preventive measures. If the violation of an obligation has already occurred or is imminent, the company must take remedial action to prevent, end or minimize the extent of the violation. In addition, in-scope companies are required to set up a complaints procedure. Finally, they must document, and publish an annual report on, the fulfilment of due diligence obligations.

What are the sanctions for non-compliance with the due diligence obligations? The competent authority, the Federal Office for Economic Affairs and Export Control (abbreviation in German: BAFA), can in particular impose a fine of up to two percent of the worldwide annual turnover of the entire group of companies. In addition, a fine of a certain minimum amount will, as a rule, lead to the exclusion from the award of public contracts for up to three years. Civil liability for the violation of the new due diligence obligations is expressly excluded. However, in particular the risk of liability under foreign law remains.

Which further rules are yet to come? To implement the SCDDA, the Federal Ministry of Labor will issue regulations and BAFA will publish guidance for companies on compliance with the law. Besides, the European Commission is expected to present a draft EU directive before the end of the year, which will probably set considerably higher standards than those under the SCDDA. All EU member states would then need to transpose the directive into their respective national law. In the case of Germany, that would mean an amendment of the SCDDA.