INITIATIVE LIEFERKETTEN GESETZ.DE

Not there yet, but finally at the start:

What the new SUPPLY CHAIN ACT delivers – and what it doesn't

An analysis by Initiative Lieferkettengesetz, 11 June 2021

Unofficial translation; original version (in German) here.

INTRODUCTION

The German "Supply Chain Due Diligence Act" is adopted! But what exactly is behind this? Our analysis shows: We are still a long way from reaching our goal in the fight against human rights violations and environmental degradation in global value chains, but with the new law, we are finally off to a good start.

The new Supply Chain Act will enter into force in 2023 and will initially apply to companies with 3,000 or more employees, then from 2024 to companies with 1,000 or more employees with a registered office or branch in Germany. The law obliges these companies to **fulfil their due diligence obligations in their supply chains with regard to respecting internationally recognized human rights and certain environmental standards**.

The law refers to the UN Guiding Principles on Business and Human Rights which are among the most important internationally recognized standards of corporate responsibility for human rights. In line with the UN Guiding Principles, the Supply Chain Act aims at strengthening the rights of people along global supply chains vis-à-vis companies.

The law is a response to the devastating incidents in which German companies have been directly or indirectly involved in their international business activities in recent years. Recurring reports about burning or collapsed factories, exploitative child labour or destroyed rainforests have shown: Voluntarily, many companies do not sufficiently fulfil their responsibility in global supply chains. Studies by the European Commission[1] and most recently by the German Government[2] have confirmed this.

Against this background, the Initiative Lieferkettengesetz was founded in September 2019 as a broad civil society alliance and has since demanded that the German Government passes a supply chain act before the end of this legislative period in September 2021. This law would have to pursue two goals:

1) Companies avoid damage to people and the environment by taking precautionary measures.

2) Affected parties can more easily obtain redress when damage has occurred.

The German Supply Chain Act passed on June 11 is a political compromise. As such, it includes a number of points that have the potential to contribute to greater human rights and environmental due diligence by companies in their value chains. At the same time, the compromise falls significantly short on many aspects, which means that the law is not effective enough and cannot just serve as a model for a European supply chain law. We shall address these points in detail in the sections "Finally at the start" and "Not there yet".

[1] https://op.europa.eu/en/publication-detail/-/publication/8ba0a8fd-4c83-11ea-b8b7-01aa75ed71a1/language-en.
[2] https://www.auswaertiges-amt.de/blob/2405080/23e76da338f1a1c06b1306c8f5f74615/201013-nap-monitoring-abschlussbericht-data.pdf

FINALLY AT THE START:

With the following points, the Supply Chain Act makes an important contribution against human rights violations and environmental degradation in corporate supply chains:

1) The law initiates an urgently needed paradigm shift in Germany - away from purely voluntary corporate social responsibility to binding human rights and environmental obligations for companies. It serves the comprehensive protection of human rights and thus paramount legal interests and enshrines due diligence by companies along the entire supply chain as a matter of principle.

2) The law unfolds a preventive effect in that companies are required to change their behaviour and prevent damage to people and the environment by taking precautionary measures. For example, they are required to comply with human rights and environmental due diligence obligations in their supply chains. This includes establishing effective risk management and conducting risk analyses systematically for their own business and direct suppliers, and on an *ad hoc* basis for indirect suppliers, in order to identify risks to people and the environment and to prevent, end or mitigate violations.

3) The law creates strong regulatory oversight and enforcement. If companies violate their due diligence obligations, they act in violation of the law and can be fined by the competent authority, the Federal Office for Economic Affairs and Export Control (BAFA), based on the severity of the offense as well as the company's total turnover. In the event of significant violations of the Supply Chain Act involving fines of at least 175,000 euros, exclusion from public procurement contracts is envisaged. The law thus provides for state actions to ensure that the due diligence obligations are actually complied with.

4) By law, affected parties can demand that BAFA takes action. If affected parties assert to the Federal Office for Economic Affairs and Export Control (BAFA) that their rights are being violated or directly threatened by a company's failure to comply with its due diligence obligations, BAFA must take action and investigate whether a breach has occurred and work towards its elimination by the company.

5) The law introduces representative action on behalf of people affected. In the future, affected parties can authorize NGOs and trade unions to raise such claims – using the already existing causes of action – on their behalf directly before German courts. This can reduce the obstacles foreign affected parties face when trying to bring claims before German courts - for example, reduce the high costs of such proceedings or guarantee anonymity in case of threatened prosecution.

6) The law regulates a few environmental obligations arising from three conventions ratified by Germany that are essentially aimed at protecting human health. These provide for the prevention of the use of persistent organic pollutants (POP Convention) and mercury emissions (Minamata Convention) as well as the control of transboundary movements of hazardous

wastes (Basel Convention). Beyond these conventions, the law covers the protected goods of soil, water and air in the context of human rights risks.

7) The scope of application and environmental obligations are more comprehensive than in the government draft bill of March 3, 2021. The law will now also cover foreign companies that have a branch office in Germany with more than 3,000 employees (more than 1,000 employees from January 1, 2024). It has also been clarified that subsidiaries belong to the parent company's own business area insofar as the parent company exercises a determining influence. And with the Basel Convention on Hazardous Waste, a third environmental convention was added to the catalogue of environmental obligations.

8) Works councils with economic committees receive new rights. When the law comes into force, they will be entitled to information and consultation on issues of corporate due diligence in supply chains in accordance with the Supply Chain Act. This will enable the elected representatives of workers' interests to work across company boundaries to strengthen social standards, human rights and environmental obligations.

NOT THERE YET:

The law has been weakened in many crucial aspects due to massive pressure from some business associations, the Christian Democratic Union (CDU) Economic Council and the Federal Minister for Economic Affairs and Energy. As a result, the law loses effectiveness and even falls behind the UN Guiding Principles in some parts. The following points contribute to the fact that the law is not effective enough:

1) The comprehensive due diligence obligations apply only to the company's own business operations and direct suppliers, but not to indirect suppliers. In the case of indirect suppliers, companies are not required to conduct a risk analysis proactively and systematically, but only on an *ad hoc* basis, when they gain "substantiated knowledge" of a potential human rights violation. This restriction is incompatible with the preventive idea of the UN Guiding Principles. It is well known that a large proportion of human rights violations occur precisely at the beginning of supply chains, i.e. in the area of indirect suppliers. Without a systematic and anticipatory analysis of possible risks, including those that are not publicly known, companies cannot adequately avoid them.

2) The law does not provide for a new cause of action in civil law holding companies liable for damage caused by failure to comply with their due diligence obligations. As a result, the legislator perpetuates judicial uncertainty. Injured parties continue to have hardly any chance of bringing claims against German companies for human rights violations before German civil courts. Moreover, the lack of a new and improved civil liability provision reduces the deterrent and thus preventive effect on companies.

3) The law takes environmental aspects into account only marginally; an independent and comprehensive environmental due diligence obligation is missing. The law limits the

environmental duties to a supposedly conclusive list of three conventions. However, such an approach is not sufficient to do justice to the prevention principle of environmental law, which is why a general clause relating to environmental damages should be introduced. Although the law so far covers the protected goods soil, water and air in the context of human rights risks, massive environmental destruction through biodiversity loss is not covered, nor is climate taken into account as a protected good.

4) The provisions on effective remediation for affected parties and on the participation of those affected in the process fall short. Effective remediation plays a central role in the UN Guiding Principles. This is not only about compensation for damages, but also about remediation as a separate component of the due diligence obligations. The law does not, however, provide for affected parties to be able to obtain redress through a complaint mechanism. Only when assessing the fine in Section 24 (4) No. 7 redress efforts by companies are taken into account. The UN Guiding Principles also require companies to consult with potentially affected groups in order to assess their human rights risks and take effective measures. This consultation with affected parties is not mandatory under the law.

5) The number of companies covered is too small. Instead of focusing on all large companies with more than 250 employees as well as small and medium-sized enterprises in sectors with particular human rights risks, the law only covers companies with more than 3,000 employees (from 2024: with more than 1,000 employees). However, small and medium-sized enterprises (SMEs) can also have significant negative impacts on human rights and environmental issues when they operate in a risk sector.

6) There are major gaps in the definition of the human rights protected when it comes to gender justice and indigenous rights. For example, gender-based violence and discrimination is not listed as an element of prohibition, although these serious human rights violations are widespread along global supply chains. Similarly, there is no reference to indigenous rights under ILO Convention 169, although Germany has just ratified this convention and indigenous peoples are exposed to particular risks from large-scale economic projects.

7) The BAFA is a federal authority under the supervision of the Federal Ministry for Economic Affairs and Energy, which has decisively blocked an ambitious supply chain law in recent months. In relation to the work of the authority, regulations must be put in place to ensure BAFA's independence from political influence by the Federal Ministry for Economic Affairs. For example, BAFA should make its decisions exclusively according to criteria of human rights and environmental due diligence and in doing so decide independently, i.e. not be subject to instructions in the processing and decision-making of individual cases. In addition, a multi-stakeholder body should accompany BAFA's work.

8) Further deteriorations compared to the government draft. Under pressure from parts of the CDU parliamentary group, a clarification was included that the Supply Chain Act does not provide for a separate cause of action in civil law. The clarification sends the wrong signal from a human rights perspective and creates legal uncertainty. The law is intended to strengthen the

rights of those affected by corporate wrongdoing. The declaratory reference that the law does not create a new cause of action for people affected contradicts this objective.

SUMMARY

The new law

- initiates an urgently needed **paradigm shift** in Germany: away from purely voluntary corporate social responsibility towards binding human rights and environmental obligations for companies.
- lays down **due diligence obligations** that are based on the UN Guiding Principles and basically cover the entire supply chain.
- imposes certain **environmental obligations** on companies.
- regulates **sound regulatory enforcement**, according to which an authority monitors compliance with due diligence obligations and sanctions non-compliance. This is intended to encourage companies to change their behaviour and take precautionary measures to avoid damage.
- partially undermines, with regard to the **scope** of due diligence, the participation of affected stakeholders in the due diligence process and **remediation**, requirements of the UN Guiding Principles.
- does not create - in addition to the specific environmental obligations - a general clause that also takes biodiversity and **climate impacts** into account.
- does **not provide for a new cause of action allowing affected parties** to more easily sue companies before German courts for damages suffered.

The Initiative Lieferkettengesetz expects the future German government to improve the law accordingly and to advocate for a supply chain law at EU level that addresses the above-mentioned weaknesses.

The 18 founding organizations of Initiative Lieferkettengesetz are: