



3 months to go: Are you ready for the German Supply Chain Due Diligence Act?

September 2022

On 1 January 2023, the German Supply Chain Due Diligence Act will enter into force. In a first step, all companies which have a specific nexus to Germany and normally employ 3,000 people or more will have to comply with newly imposed due diligence obligations aimed at minimising the risk of infringements of human rights and environmental standards. Suppliers to such companies are already being asked to comply with similar obligations irrespective of whether the law currently applies to the suppliers themselves. In any case, the law will also become directly applicable to German companies normally employing 1,000 people or more as of 1 January 2024.

Whichever date is applicable in the individual case, the fact that the German Supply Chain Due Diligence Act will presently apply should prompt companies to consider the latest developments relating to product and supply chain regulations that unanimously aim to promote sustainability, environmental protection and human rights – all of which are highly critical issues for both companies and investors when addressing ESG strategies.

German Supply Chain Due Diligence Act – German companies & extra-territorial effect

The German Supply Chain Due Diligence Act must be observed by companies, regardless of their legal form, that have their seat or headquarters in Germany and normally employ at least 3,000 people in Germany. This threshold will be lowered to 1,000 employees as of 1 January 2024.

As regards the employee thresholds, however, the law provides somewhat ambiguous **aggregation rules that need to be taken into account in corporate groups and holding structures** including typical Private Equity structures. Basically, these aggregation rules require that each German company within a corporate group structure is identified. It is then necessary to assess whether any of these companies qualify as affiliated companies in terms of section 15 of the German Stock Corporation Act (*Aktiengesetz – AktG*). The number of the people employed by such companies must be aggregated at the level of the respective German company that exercises relevant control over the controlled entities. The controlled entities will have to comply with the German Supply Chain Due Diligence Act whenever their respective parent company is directly subject to the law (i.e. where that entity has 3,000 / 1,000 or more employees) or because the controlling entity exercises decisive influence (*bestimmender Einfluss*) over the controlled entity.

The German Supply Chain Due Diligence Acts also provides for **extra-territorial effect**:

- Branches operated in Germany by non-German companies explicitly qualify as German companies in terms of the law.
- Within corporate groups, German controlling entities will have to ensure that any non-German companies over which they exercise decisive influence pursuant to the (legally non-binding) guidance issued by the competent regulator, the German Federal Office for Economic Affairs and Export Control

(*Bundesamt für Wirtschaft und Ausfuhrkontrolle – BAFA*), also comply with the law.

- German companies will have to ensure that both their direct and indirect suppliers comply with the regulations. It is therefore likely, and a corresponding trend is already clearly visible in the market, that German companies will require that their suppliers comply with the standards imposed by the German Supply Chain Due Diligence Act irrespective of the origin and location of those suppliers.

What needs to be completed by 1 January 2023?

On 1 January 2023, companies that are subject to the German Supply Chain Due Diligence Act should have:

- conducted an **appropriate due diligence** focussing on risks relating to the infringement of human rights and environmental standards as defined by the German Supply Chain Due Diligence Act in detail;
- established an effective and specific **risk management system**, which may be integrated into that company's or corporate group's broader compliance management system;
- appointed an individual who is responsible for compliance with the German Supply Chain Due Diligence Act ("**Business Human Rights Officer**");
- established a **complaints procedure**;
- ensured the relevant internal **documentation** is kept, particularly regarding the due diligence.

If risks are identified in the course of the company's due diligence, additional measures must be implemented. Such measures should include appropriate **contract language** with suppliers. Such language may, as a last resort, include a right to terminate the contract if infringements of human rights and environmental standards cannot be halted.

The proper documentation of such measures will be key to **minimising potential litigation risks**. This

also applies to cases where companies decide not to take any additional measures, since the German Supply Chain Due Diligence Act provides for the possibility of NGOs to assert claims based on the violation of human rights related duties.

External **reporting obligations**, as stipulated specifically by the German Supply Chain Due Diligence Act, must have been complied with no later than 4 months after the end of the first financial year ending after 1 January 2023 – i.e. depending on the end of the financial year of a German company, the first reports pursuant to the German Supply Chain Due Diligence Act will already need to be published in April or May 2023.

It should be noted that the German Supply Chain Due Diligence Act requires that a specific report is prepared, i.e. **it will not be sufficient to integrate such report into the company's annual report**. This represents an add on to the usual non-financial reporting obligations that already form part of a company's annual report. The report must include: (i) any human rights related or environmental risks identified, (ii) any measures undertaken towards fulfilling the due diligence obligations under the German Supply Chain Due Diligence Act, (iii) an evaluation of the effectiveness and impact of such measures and (iv) any conclusions derived for future measures. Business secrets must be duly protected and do not need to be disclosed.

The failures to comply with the requirements stipulated in the German Supply Chain Due Diligence Act not only expose companies to **reputational risks**, but may also lead to high administrative fines and even the **exclusion from public procurement procedures**. In particular, BAFA can impose **administrative fines** of up to EUR 800,000 or of up to 2% of the yearly worldwide turnover in respect of companies with a yearly turnover of more than EUR 400 million. Again, the proper documentation of measures will be important to mitigate potential enforcement risks.

More guidance to come

The German Supply Chain Due Diligence Act frequently refers to legal concepts such as “effectiveness” and “appropriateness”. While this allows for some flexibility on the one hand, at the same time it triggers a degree of legal uncertainty. The legislator has expressly empowered the **competent regulatory authority to provide guidance** in the form of (legally non binding) “handouts” (*Handreichungen*). However, the BAFA has not yet published any comprehensive guidance except for:

- a catalogue of Frequently Asked Questions (FAQs)¹;
- a paper outlining the key principles for an adequate risk assessment²;
- a relatively vague text elaborating on the principles of “effectiveness” and “appropriateness”³.

The BAFA has further stated that a template questionnaire will be published which is to be used in order to comply with the external reporting obligations.

It is expected that the BAFA will publish more guidance but it is currently unclear when such guidance will be publicly available.

Reactions in the market – best practice considerations

In our opinion, all companies must carefully consider (i) what they are mandatorily **obliged** to do, (ii) what their stakeholders, including shareholders, customers, employees etc., **expect** them to do and (iii) what the companies themselves are **willing** to do over and above this, in order to improve their ESG scoring, for instance.

In this context, it is advisable for companies to have a reliable legal analysis performed to ascertain whether or not they are subject to the German Supply Chain Due Diligence Act. This should cover

¹ In German only: [Das Lieferkettengesetz im Überblick](#)

² In German only: [Risikoanalyse](#)

³ In German only: [Angemessenheit und Wirksamkeit](#)

whether the employee aggregation rules apply and explore the legal structure of corporate groups comprising German companies or companies operating branches in Germany.

Many companies that will not themselves be directly subject to the German Supply Chain Due Diligence Act are currently reviewing their customer base and facing **requests from their customers** to implement measures equal or at least similar to the obligations imposed by the German Supply Chain Due Diligence Act insofar as such customers are required to comply with these standards and, thus, need to ensure that their suppliers do not trigger any relevant concerns in terms of human rights and environmental standards.

Other companies are implementing standards equal or similar to those stipulated in the German Supply Chain Due Diligence Act on a purely voluntary basis in order, for instance, to evidence their commitment to human rights and environmental standards and/or to improve their **ESG scoring** in line with one of the still very few legal benchmarks in this sector.

Emerging supply chain and product related legislation

The German Supply Chain Due Diligence Act should be viewed in the context of a number of other **legislative developments that also aim to promote supply chain and product related regulations** by using legislation as an instrument for furthering human rights, environmental standards and sustainability topics more generally. Examples include:

- The Norwegian Transparency Act⁴, as one of the most recent examples of supply chain due diligence acts similar to the German Supply Chain Due Diligence Act, or the French “*Loi de Vigilance*”.

- The EU proposal for an EU wide Directive on corporate sustainability due diligence⁵.
- The EU proposal for a Regulation on deforestation-free products⁶.
- The EU proposal for a Critical Raw Materials Act⁷.
- The EU proposal for a Regulation on prohibiting products made with forced labour on the Union market⁸ – an instrument quite similar to the US Uyghur Forces Labour Act.

In addition, the EU plans to enact new rules on non-financial reporting obligations through its Corporate Sustainability Reporting Directive (CSRD)⁹.

Related regulations on “sustainable” products

In this context, please also refer to our previous publications and alerts relating to:

- The German Supply Chain Due Diligence Act: Part 1 – [Introduction](#); Part 2 – [Compliance](#); Part 3 – [Litigation](#); Part 4 – [FAQs](#)
- [The ninth edition of our Business and Human Rights Review](#)
- [The European Commission's new proposal to keep the EU free from forced labour](#)
- [Recent developments in European Business and Human Rights \(BHR\) litigation](#)
- [The European Commission's proposal for a directive on corporate sustainability due diligence](#)
- [Corporate vigilance and accountability in Belgium](#)

⁴ [Act relating to enterprises' transparency and work on fundamental human rights and decent working conditions \(Transparency Act\)](#)

⁵ [Just and sustainable economy: Commission lays down rules for companies to respect human rights and environment in global value chains](#)

⁶ [Proposal for a regulation on deforestation-free products](#)

⁷ [Critical Raw Materials Act: securing the new gas & oil at the heart of our economy | Blog of Commissioner Thierry Breton](#)

⁸ [Commission moves to ban products made with forced labour on the EU market](#)

⁹ [New rules on corporate sustainability reporting: provisional political agreement between the Council and the European Parliament](#)

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