IN sights

April 2022:

„Corporate Sustainability Due Diligence“

Before the Supply Chain Duty of Care Act (LkSG) comes into force, the EU is once again tightening the requirements.

In February 2022, the European Commission adopted a proposal for a directive "on corporate sustainability obligations". The proposal aims to "promote sustainable and responsible corporate behaviour in all global value chains".

With the newly proposed directive, the EU Commission is pursuing the goal of obliging companies along the entire value chain to comply with human rights and environmental protection. The draft apparently provides for stricter regulations than the so-called Supply Chain Security Act (LkSG), which will come into force in Germany from January 2023.

For the time being, the draft does not have any binding effects on national (German) law, as it must first be adopted by the EU Parliament in Strasbourg and the EU Council. But it can be assumed that the Bundestag will then adapt the LkSG accordingly, i.e. tighten it up.

EU proposal covers entire supply chain

What is striking about the proposed tightening is the expansion of the due diligence and monitoring obligations by the companies concerned. While in the LkSG version this refers primarily to direct suppliers within the supply chain, the EU proposal explicitly extends to the entire supply chain. In a first step, these requirements will cause a considerable additional administrative effort and will certainly also lead to an increase in costs in the area of insurable risks.

Large parts of the medium-sized industry in Germany included

A key point of the tightening would be that the EU Commission's proposal, in contrast to the LkSG that will apply in Germany from 2023, contains a civil liability clause. This would enable aggrieved private individuals (e.g. in the case of human rights violations) to sue companies for abuses at certain points in the company-specific supply chain.

And while the LkSG only applies to companies with 3,000 or more employees (and from 2024 also to companies with 1,000 or more employees), the direct scope of the European Supply Chain Act would already apply to companies with 500 or more employees if their annual turnover exceeds €150 million. Even more: For companies operating in so-called "risk sectors or resource-intensive sectors" such as the textile industry, an annual turnover of 40 million p.a. is sufficient if more than 250 employees are employed. This means in effect that very large parts of medium-sized industry in Germany will be included in the scope of the possible tightening.

Establishment of supplier management

In our view, however, this is no reason for panic or exaggerated actionism. The implementation of the LkSG will in any case lead to more or less all companies involved in the market adapting their structures accordingly with regard to supply chain transparency, contract design and control mechanisms. This will also affect small businesses insofar as they are suppliers

to larger companies that fall directly within the scope of the LkSG.

By properly setting up supplier management processes in a company, this additional administrative burden can be significantly reduced and controlled. Many of these processes can be supported by digital tools and facilitate the legally required reporting (annual publication as part of a corresponding report).

Being prepared for the entry into force

Even for companies that are not yet sufficiently positioned in this area, far-reaching solutions can be neatly prepared and successively implemented over a longer period of time. From our experience, however, it is important not to wait until the laws and regulations come into force, but to prepare (calmly) for them now (practice-oriented risk management, transparent purchasing processes and guidelines, and a revision or development of compliance structures). However, it becomes time-consuming and critical for market participants if they try to transfer supposed standard solutions to the specific needs of their company at the last minute.

Author
Gregor van Ackeren
Managing Director