

German Supply Chain Act: Due Diligence Obligations Explained

Guide

In this article, you will learn about the German Supply Chain Act and what it means for businesses in Germany and around the world.

The Supply Chain Act at a glance:

- The German Supply Chain Act is the first legislative step that obliges companies established in Germany to protect people and the environment harmed by their global supply chain operations.
- From 2023, the Act initially applies to enterprises with at least 3,000 and, from 2024, additionally to enterprises with at least 1,000 employees in Germany.
- The Federal Office for Economic Affairs and Export Control (Bundesamt für Wirtschaft und Ausfuhrkontrolle) will be equipped with effective enforcement instruments to monitor an enterprise's supply chain management.
- Fines can amount to up to 8 million euros or up to 2% of annual global turnover.

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Introduction

In June 2021, the German legislature passed the “Gesetz über die unternehmerischen “Sorgfaltspflichten zur Vermeidung von Menschenrechtsverletzungen in Lieferketten” (German Supply Chain Act). The German Supply Chain Act (GSCA) carries new rules to ensure companies doing business in Germany meet the standards set out in United Nations (UN) Guiding Principles on Business and Human Rights and the OECD Guidelines for Multinational Enterprises.

The law imposes due diligence obligations on companies that have a principal place of business, administrative headquarters, statutory seat, or branch office in Germany to comply with human rights and environmental standards. It also exposes them to serious liabilities upon violations.

The German Supply Chain Act provides a comprehensive list of obligations including the establishment of a risk management system for compliance. It also outlines the necessary preventive and remedial measures, makes complaint procedures mandatory and requires regular documentation and reports.

In this article, you will learn about the German Supply Chain Act and what it means for businesses in Germany and around the world.

01

What is a supply chain in this context?

The supply chain within the meaning of the German Supply Chain Act refers to all products and services of an enterprise. It includes all steps in Germany and abroad that are necessary to produce the products and provide the services, starting from the extraction of the raw materials to the delivery to the end customer and includes:

1. the actions of an enterprise in its **own business area**,
2. the actions of **direct suppliers** and
3. the actions of **indirect suppliers**.²

46%

Of consumers want more clarity on the sourcing of products.

Source: Deloitte

28%

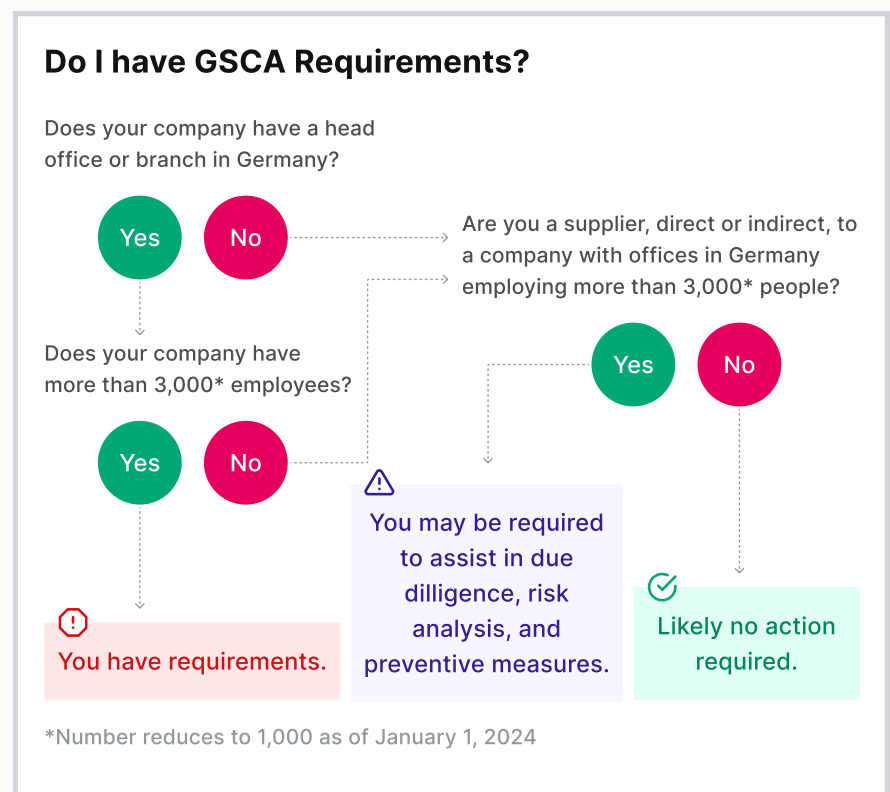
Of consumers stopped purchasing certain brands or products because of ethical or sustainability related concerns about them.

Source: Deloitte

2%

The fines upon non compliance with the GSCA requirements can amount up to €8 million or 2 % of the average annual turnover.

Source: GSCA



The scope of the German Supply Chain Act

From 2023: Companies based in Germany with more than 3,000 employees, or German-registered branches of foreign companies with more than 3,000 employees. This concerns approximately 600 companies.

From 2024: Companies based in Germany with more than 1,000 employees, or German-registered branches of foreign companies with more than 1,000 employees. It will concern approximately 2,800 companies, according to the Explanatory Memorandum on the Supply Chain Act.

→ Own business area

However, even if your own company does not reach the thresholds mentioned, you can expect small and medium-sized enterprises (SMEs) to be affected as well, since the large companies addressed will likely pass on the due diligence obligations imposed on them by law to their suppliers. In future, smaller companies will also be covered by the "sphere of influence" of the German Supply Chain Act without themselves being in-scope companies.

→ Direct suppliers

Under the German Supply Chain Act, companies must monitor and act upon violations in their own operations, as well as operations of their direct suppliers worldwide starting from the extraction of the raw materials to the delivery to the end customer.

→ Indirect suppliers

In addition, if companies obtain substantiated knowledge of a possible violation of human rights or environmental standards by one of their indirect suppliers, they must immediately conduct a risk analysis for these violations.

03

What does the German Supply Chain Act apply to?

The regulation defines two major protected legal positions: the **environment** and **human rights** ⁴

ENVIRONMENTAL RISKS

An environment-related risk within the meaning of this Act is a condition in which, on the basis of factual circumstances, there is a sufficient probability that one of the following prohibitions will be violated:

Minamata Convention on Mercury	<ul style="list-style-type: none">• Manufacture of mercury-added products• Use of mercury and mercury compounds in manufacturing processes• Insufficient treatment of mercury waste
Stockholm Convention on Persistent Organic Pollutants (POPs Convention)	<ul style="list-style-type: none">• Production and use of prohibited chemicals• Handling, collection, storage and disposal of waste in a manner that is not environmentally sound
Basel Convention of the Control of Transboundary Movements of Hazardous Wastes and their Disposal	<ul style="list-style-type: none">• Exports and handling of hazardous waste

HUMAN RIGHTS RISKS

A human rights risk, as defined by this Act, is a situation in which, based on factual circumstances, there is a reasonable probability that one of the following prohibitions is violated:

<ul style="list-style-type: none">• Child labor• Worst forms of child labour• Forced labour• Slavery• Occupational safety and health obligations• Freedom of association• Unequal treatment/discrimination	<ul style="list-style-type: none">• Adequate Living Wage• Environmental Damage & Excessive Water Consumption• Unlawful Eviction and Taking of Land, Forest, Water• Inappropriate Use of Security Forces• Act or omission in breach of duty to act that goes beyond points 1 to 11 and the unlawfulness of which is obvious upon reasonable assessment of all the circumstances in question.
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How to comply with the German Supply Chain Act due diligence obligations?

The highlight of the new German Supply Chain Act is the obligation for companies to conduct human rights and environmental due diligence. The due diligence obligations include nine high-level requirements:

1. Establish a risk management system

Companies must create an appropriate risk management system to comply with the German Supply Chain Act obligations. As part of their risk management, companies must first analyse their own human rights and environmental risks and the identical risks of their direct suppliers.

2. Define in-house responsibility for compliance

Companies are required to appoint a “human rights officer” who is responsible for monitoring the risk management within their supply chains. This does not necessarily have to involve creating a new job or hiring new employees, as risk management tasks can be integrated into existing departments (e.g. compliance officer, sustainability department, etc.). Additionally, senior management must also be informed about the work of the responsible person at least once a year.⁵

3. Perform regular risk analyses

The risk analysis must be carried out by companies at least once a year and on an ad hoc basis, for example due to the introduction of new products, projects or a new business field.⁶

4. Issue a policy statement

In-scope companies must issue a policy statement that includes the following elements of a human rights strategy:

- Describe the procedures by which the company fulfills its German Supply Chain Act obligations.
- Describe the company's priorities related to human rights and environmental risks.
- Share expectations placed by the enterprise on its employees and suppliers.

The statement assures that the company's board and management are fully committed to its human rights agenda.

5. Establish preventive measures in your own business area and for direct suppliers

Companies must implement appropriate procurement and purchasing practices, deliver training in relevant business areas, and establish control measures to verify compliance with the human rights strategy outlined in the policy statement.

6. Take remedial action

If the company determines that a violation of a protected legal position has occurred or is imminent, it must immediately take appropriate remedial action to prevent, stop or minimise the violation. Failure to do so may result in not just fines, but also civil action by harmed parties, NGOs, and even competitors.⁷

If the violation cannot be stopped in the foreseeable future, the company must outline and carry out a concept to end or minimise the violation without delay. The company must consider the following measures:

- Outline a concrete timetable.
- Work on minimising the violation together with the company that caused it.

- Temporarily suspend its relationship with the supplier while efforts are made to minimise the risk.

Termination of business relationships is only required as a last resort in the event of serious human rights violations by suppliers that cannot be remedied in any other way.

The effectiveness of the preventive and corrective measures must be reviewed annually and on an ad hoc basis in the event of a significant change in the risk exposure profile such as the introduction of new products, projects or a new field of business.

7. Establish a complaints procedure

In-scope companies must establish a complaints procedure to enable people to report violations of human rights- or environmental- related obligations in their own business area or that of a direct supplier. The procedure should be publicly available. A person submitting the complaint should be informed of its reception. The effectiveness of the complaints procedure must be reviewed annually and on an ad hoc basis when necessary.

8. Implement due diligence obligations with regard to risks at indirect suppliers

If a company has substantiated knowledge of its indirect supplier's misconduct, it must immediately address the risks, outline and implement preventative measures, and update its policy statement, if necessary.

9. Document and report on due diligence activities

A company must report on the fulfilment of its due diligence obligations annually. It must make the report publicly available free of charge on the company's website no later than four months after the end of the financial year for a period of seven years.

Consequences and penalties for non-compliance

The implementation of the due diligence obligations laid down in the German Supply Chain Act is monitored by the German Federal Office for Economic Affairs and Export Control (Bundesamt für Wirtschafts- und Ausfuhrkontrolle or BAFA). If a company fails to comply with the due diligence obligations pursuant to the German Supply Chain Act, the Act provides the following sanctions:

1 Fines

Periodic penalty payments of up to EUR 50,000 in administrative enforcement proceedings and/or fines. The fines can amount to up to EUR 8 million. In case an average annual turnover of a company is more than 400 million euros, the fine can go up to 2% of the average annual turnover

2 Exclusion from public tenders

Upon violation, companies can be excluded from winning public contracts in Germany for up to three years.

3 Civil liability

Claims under section 823 of the German Civil Code (Bürgerliches Gesetzbuch - BGB)⁸ on the grounds of a breach of a duty of care and claims under foreign law are a realistic threat to German companies violating human rights.

While liability may not have been extended in substantive legal terms, it has been in procedural terms. The German Supply Chain Act now extends the rights of domestic trade unions and non-governmental organisations (NGOs) regarding the assertion of third party rights violations in front of German courts.

Thus, a person claiming to be the victim of a violation of a "paramount protected legal position" may authorise trade unions and NGOs to bring proceedings to enforce that person's rights in their own capacity (i.e. "special transfer of procedural authority").⁹

The future of Due Diligence regulations

Mandatory supply chain due diligence and reporting is becoming the norm in Europe.¹⁰ In addition to Germany, the Netherlands, France, Switzerland, Norway and other countries now require elements of due diligence. These include the:

- [Dutch Child Labour Due Diligence Law](#)
(this law is supposed to come into force in 2022)
- [Norwegian Transparency Act](#)
- [Swiss Due Diligence Law](#)
- [French Duty of Vigilance Act](#)

Next to this, in March 2021, the European Parliament passed a resolution in which it requested the European Commission to submit a legislative proposal on mandatory supply chain due diligence. This will then become a unifying supply chain due diligence process that will take precedence over the national due diligence laws that are already being implemented.

EU Justice Commissioner Reynders stated: "We want to go a long way, a long way down the supply chain and a long way in terms of the number of companies involved."

Next steps

→ FOR OEMS AND BRANDS

- The most important first step to prepare for the German Supply Chain Act is to map all your direct suppliers.
- Work with your procurement and buying teams to create a full list of your direct suppliers.
- Conduct a basic risk assessment, considering their locations, the nature of their businesses, the types of people they employ and the conditions they provide.
- Last, collect contact details for each supplier in case of an emergency.

→ FOR SUPPLIERS

- Check that you are compliant with labour, health and safety and environmental regulations.
- Read into the German Supply Chain Act and what it requires companies to do. Learn about the information your customers will need from you.
- Make sure your paperwork is up-to-date and ready to share with customers to help them comply with the new law. This will help you build stronger relationships with brands and OEMs.

Conclusion

Today, supply chains extend around the entire world. For decades, international corporations have been criticised for not complying with human rights and environmental standards along their supply chains and for profiting from poorly enforced national regulations in emerging and developing countries.

The German Supply Chain Act is the first legislative step that obliges companies established in Germany to protect people and the environment harmed by their global supply chain operations.

To avoid liability, companies must comply with the standards outlined in the German Supply Chain Act. The due diligence obligations include nine high-level requirements: establishing a risk management system, assuring in-house responsibility for compliance, performing regular risk analyses, issuing a policy statement, establish preventive measures for their own business and for direct suppliers, taking remedial action when necessary, establishing a complaints procedure, implementing due diligence obligations with regard to risks at indirect suppliers, and documenting and reporting on due diligence activities. These activities should be done on an annual basis or upon request.

Ensuring compliance with the new regulations can be a daunting task. However, with implementation of digital technologies for supply chain traceability you can make it easier. Circularise is one of the solutions that can help you with compliance.

Here's what some of our customers say about us:



With the help of Circularise, as well as with the help of their partners we were able to trace for a number of specific cases plastics from raw material production to the final car."



Antoon Versteeg -
Project Lead Innovation
Research, Porsche



Circularise helps us to maintain this confidentiality and only disclose the information needed from raw material producer to recycler. And with that, we can close the loop."



Uwe Peuker - Vice President
Regional Product Management
Polycarbonates, Covestro



Circularise Plastics is building a data-exchange protocol with privacy at its heart, which we believe is a smart strategy as privacy concern is what often refrains companies from becoming more transparent."



Thomas Nuyts - Global
Product Manager, Domo

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Circularise's Software system helps suppliers in chemicals and plastics, battery materials, metals, and other industries to trace and share material data including bill of materials and environmental data without risking their sensitive information.

By extension, it helps brands and OEMs to monitor their supply chains, get visibility into their own Scope 3 emissions, comply with upcoming due diligence regulations, and implement the circular economy in their operations

To contact us, simply go to the link below!

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[in](#) [t](#) [M](#)

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Traceable supply chains for a circular economy

Circularise's Software system helps suppliers in chemicals and plastics, battery materials, metals, and other industries to trace and share material data including bill of materials and environmental data without risking their sensitive information.

By extension, it helps brands and OEMs to monitor their supply chains, get visibility into their own Scope 3 emissions, comply with upcoming due diligence regulations, and implement the circular economy in their operations.

