



# **SUPPLY CHAIN ACT (LKSG)**

Status quo and the impact on the implementation in German companies. Joint study by Ansbach University of Applied Sciences and EQS Group



# EXECUTIVE SUMMARY

**A**s of Jan. 1, 2023, around 700 companies were affected by Germany's Supply Chain Act (LkSG). As of Jan. 1, 2024, the law's threshold will drop to 1,000 employees, meaning that around 2,900 companies are expected to fall within the regulation's scope.

The LkSG obliges these companies to set up a management system to comply with human rights and environmental due diligence requirements for their own business operations, for direct suppliers and throughout the supply chain.

In part, the human rights due diligence obligations are reminiscent of elements that many companies have already anchored in practice through classic compliance management systems (CMS for short) to avert risks. The LkSG now regulates the introduction of an appropriate and effective supply chain CMS for the first time and sets out requirements for its design.

Similar to the due diligence obligations, which are to be understood as a continuous cycle of procedural steps that build on and refer to each other, a CMS as defined by IDW PS 980 also provides for a repetitive sequence of elements that interact with each other. In order to meet their responsibilities and at the same time minimize the effort associated with the new obligations, it makes sense for companies to use existing systems when implementing the due diligence obligations. Due to the open design of the seven basic elements of an effective CMS according to IDW PS 980, such a system can be adapted to the individual company and therefore enables the integration of new legal areas. This may sound simple, but it poses major challenges in the implementation of the due diligence requirements according to the LkSG.



## Key Findings



**Companies perceive the LkSG as an additional burden with a high level of bureaucracy:** The increasing regulation in the area of compliance burdens companies as they often lack the financial and human resources to implement the legal obligations.



**Companies usually use existing structures and systems, such as a compliance management system, to implement the human rights due diligence obligations:** The companies usually carried out a gap analysis for the implementation of the LkSG due diligence obligations in order to be able to implement the requirements in compliance with the law using board resources. The project teams for implementing the LkSG requirements usually consist of the Compliance and Purchasing departments and perform this activity in addition to their existing tasks.



**There is uncertainty and a lack of clarity regarding the implementation of LkSG requirements:** Companies complain about unclear legal terms as well as specifications with which they can orient themselves when implementing the LkSG requirements. This goes hand in hand with the fear of being fined.



**The human rights officer - an unloved job?** Companies find it difficult to fill the position of human rights officer. Due to liability, existing functions are skeptical about taking on this officer role.



**The due diligence obligations of the LkSG are often passed on through contractual obligations in the supply chain ("trickle down" effect):** Companies lack insight into their supply chain. This is complemented by a lack of understanding of the LkSG duties of care by business partners, so that companies see the contractual obligation as a last resort for prevention.



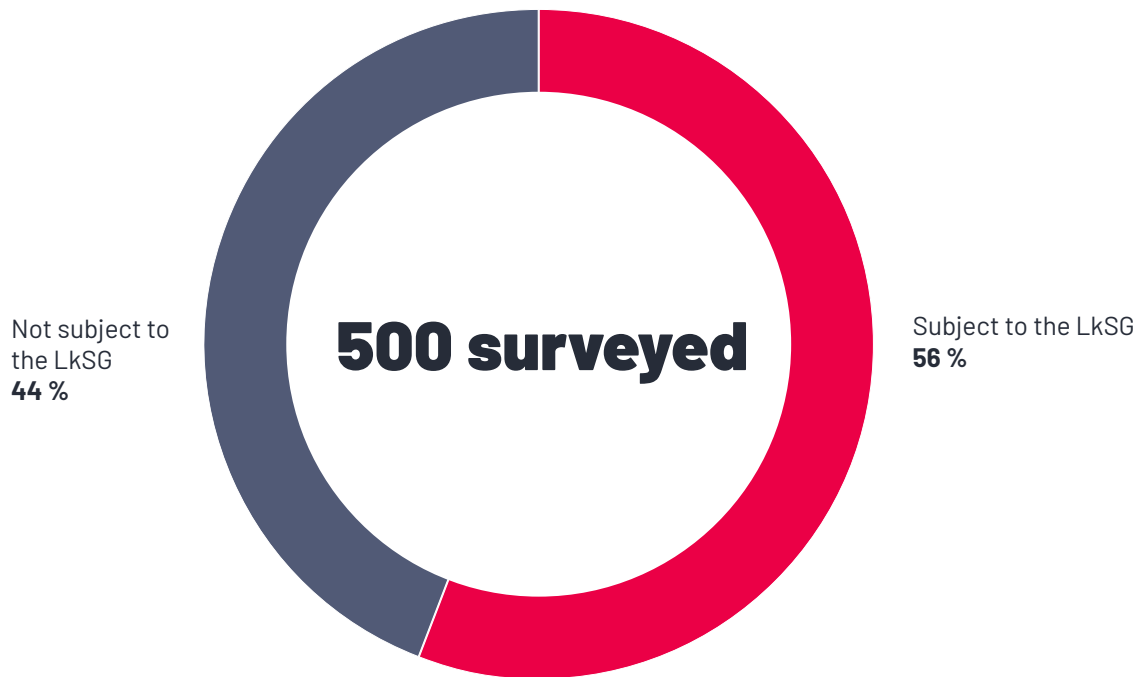
**An effectiveness check on the degree of implementation of the due diligence obligations under the LkSG is not currently the focus of companies:** Organisations are still facing the challenges of implementing LkSG requirements in their business.



**Concerns about more far-reaching EU legislation on human rights due diligence:** Companies are looking with concern at the "Corporate Sustainability Due Diligence Directive". They fear significantly stricter regulations than those provided for by the LkSG.

Together with EQS Group, Ansbach University of Applied Sciences is publishing its first report on the LkSG. This study relates to companies based in Germany and sheds light on the following questions: Where do German companies stand regarding the implementation of the due diligence requirements of the LkSG? What are the implications for German companies?

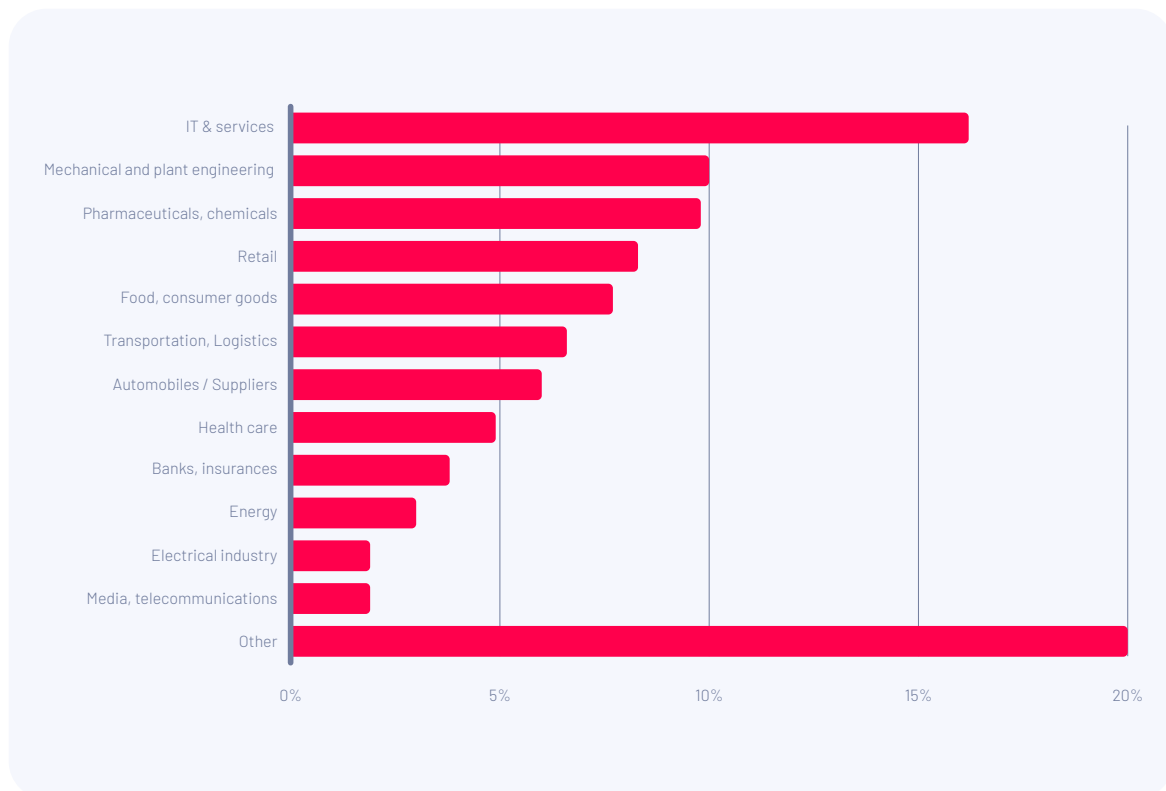
The analyses are based on data obtained using a “mixed methods” approach. For this purpose, representatives of 500 companies selected on a representative basis according to sector, number of employees and turnover were asked about their experience with the implementation of the LkSG. In the sample, care was taken to ensure a balanced relationship between companies subject to the LkSG (56%) and those not subject to the LkSG (44%). Where necessary, the study differentiates between these two groups.



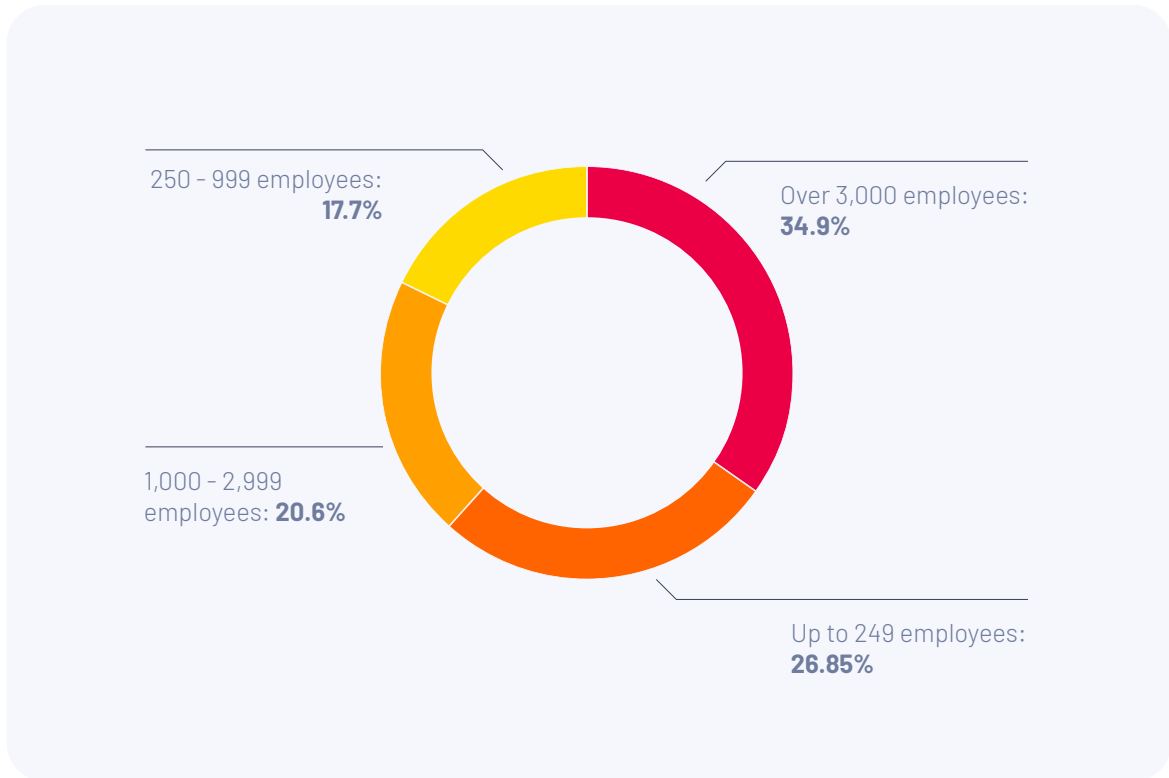
# PARTICIPANT STRUCTURE

Overall, companies with the following structural distribution participated in the study:

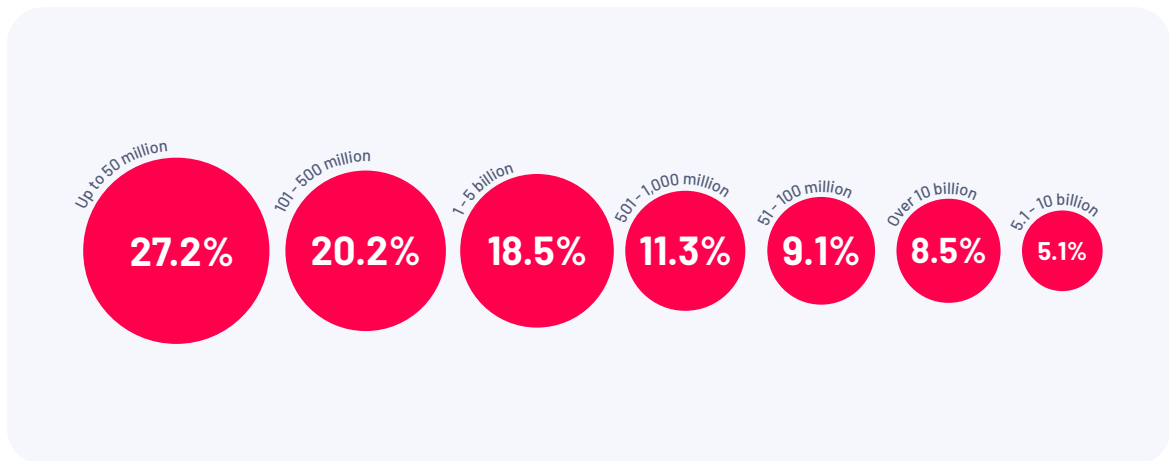
**Which industry does your company belong to? (n=470)**



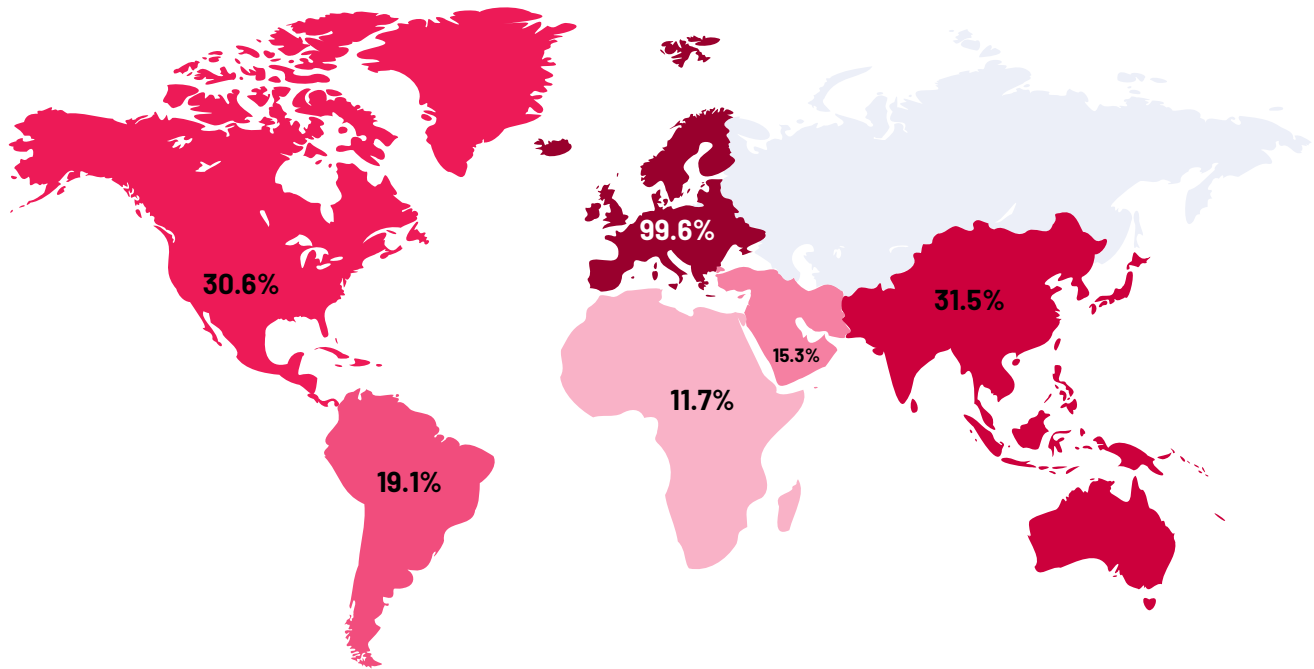
### How many employees work in your company? (n=470)



### What is the turnover of your company? (n=470)



**In which regions does your own business unit have a location? (n=470)**







# CONCLUSION

**T**he present results of this field study make it clear that many of the companies surveyed are very critical of the LkSG. This attitude is absolutely understandable and many concerns are justified. After all, the implementation of the Supply Chain Sourcing Obligations Act is indisputably a very complex task that demands time, competencies and resources from companies.

On the other hand, the LkSG offers companies the opportunity to make their supply chains more sustainable and thus make a positive contribution. The Act offers the opportunity to improve one's own sustainability strategy and strengthen a competitive position. In doing so, it seems sensible to first use existing resources with an agile approach and to successively integrate them into existing structures and processes.

As with other laws, the LkSG requires clear responsibilities and this often newly created function finds itself in an interdisciplinary, coordinating role.

Responsible parties are required to communicate with internal and external stakeholders. At the same time, a comprehensive knowledge of internal processes is required to operationally implement due diligence in all facets.

Ultimately, organizational structures in many companies are in place and not very dynamic. They remain as preparation to increase professional empowerment and to drive the digitization of processes through pragmatic solutions.



In addition to a digital whistleblowing system that meets the requirements of the complaints procedure, this also includes tools for risk analysis and business partner auditing, including evaluation. These workflows can be mapped just as efficiently as the assignment of responsibilities or the documentation and deletion concept, in which the special retention obligations of the LkSG must be observed. But preventive measures can also be managed digitally. For example, it is possible to check and document which supplier has accepted the supplier code of conduct adapted to the LkSG and when. Here, it is advisable to deal with the selection of tools at an early stage in order to be able to take their special features into account when designing the compliance processes.

Do you have any general questions about the study and the results, or do you need support when it comes to the practical implementation of the LkSG?

Then please feel free to contact us!

**The complete report available in German**

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# ABOUT EQS GROUP AG

EQS Group's products are bundled in the cloud-based software EQS COCKPIT. This allows compliance processes in the areas of whistleblower protection and case handling, policy management and approval processes to be managed just as professionally as business partners, insider lists and reporting obligations.

Listed companies also benefit from a global newswire, investor targeting and contact management, as well as IR websites, digital reports and webcasts for efficient and secure investor communication.

In addition, EQS Group develops software for the management of ESG (environment, social, governance) data, the fulfilment of human rights due diligence obligations along corporate supply chains and for rule-compliant sustainability reporting. EQS Group was founded in Munich in 2000. Today, the group employs around 600 professionals and is represented in the world's most important financial centres.



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