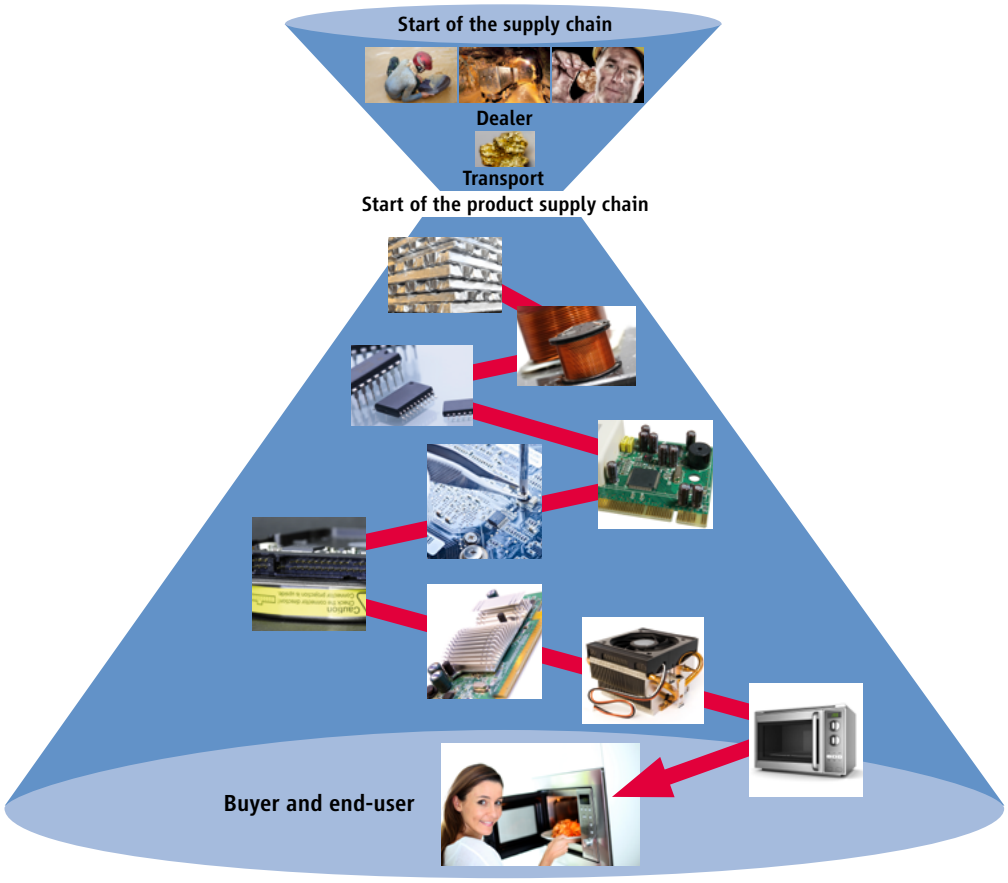
ZVEI:
Die Elektroindustrie

Position statement by the German Electrical Industry on the planned European regulation of supply chain due diligence



German Electrical and Electronic Manufacturers' Association

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Position statement by the Electrical Industry on the planned European regulation of supply chain due diligence

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Major concerns

Problem

- In some regions of the world, there is a risk that the protection of internationally recognised human rights and the environment will be disregarded in the production or processing of goods.
- The electrical industry fully supports the protection of human rights and the environment, as well as the prevention and containment of armed conflicts and crisis situations in third countries.
- It is the task of the European Union to pursue a coherent foreign, security and development policy. In accordance with the UN Guiding Principles on Business and Human Rights (UNGP), companies can make a supplementary contribution in their own sphere of responsibility, but cannot replace decisive political action.

Principal arguments

- Companies need clear, explicit statutory stipulations with a binding definition of the necessary action framework.
- Companies need legally binding, workable instruments (compliance tools) in order to cope with continuous control of the supply chains .
- Companies need the support of the EU and the EU Member States to put supply relationships and supply chains on a legally certain footing.
- Safeguarding supply chains requires a legal basis in order to impose corresponding obligations on suppliers in non-European countries.

Proposal

The companies in the electrical sector are European companies in a European market. They have branches and production facilities and thus also identical supply chains in nearly all EU Member States. The regulations must therefore also be identical in all EU Member States. Only a European Regulation can prevent a patchwork of stipulations and create a level playing field in Europe, thus ensuring joint effective action abroad.

Establishment of a European regulation on supply chain due diligence must make individual national regulations in the Member States null and void.

The electrical industry proposes a fourfold approach that brings together the state with its task of a coherent foreign, security and development policy and the industry with its global business activities:

1a. Merger of the planned due diligence regulations with the already existing European due diligence regulations, e.g. the existing Conflict Minerals Regulation (EU) No. 2017/821, the Timber Regulation (EU) No. 995/2010 and the Council Regulation (EU) 2020/1998 of 7 December 2020 concerning restrictive measures against serious human rights violations and abuses, to avoid parallel due diligence obligations with requirements of differing content in identical supply chains.

1b. Stipulation of the other supply chain due diligence requirements by means of a Regulation, not a Directive, to avoid a patchwork of different stipulations.

2. **Obligation for market participants to oblige** the supply chain suppliers to comply with human rights and international standards at work and in the environment and also e.g. to use minerals from areas not affected by conflict pursuant to the EU Regulation on conflict minerals.

3a. Creation of a **„Human Rights Negative List"**[2] by the legislator with a list of companies and individuals that have systematically violated human rights and human dignity. This provides companies with an instrument to identify critical business partners. N.B.: Such an instrument already exists in the EU. Besides the Council Regulation (EU) 2020/1998, there are already 46

[1] Supply chain is the generic term. However, the political sector always understands this to refer to what is known as the value chain which also covers e.g. services and financial services

[2] „Human Rights Negative List" as working title. Abbreviation: HRNL

EU sanctions regulations that companies are obliged to check and comply with, including sanctions for human rights violations.

3b. **The European Union obliges companies, authorities and state institutions to check the „Human Rights Negative List".**

3c. **Consequences** against companies and individuals stated in the **„Human Rights Negative List"** could include:

- Business relations are prohibited with companies and individuals stated in the „Human Rights Negative List".
- Companies and their suppliers exclude such companies and individuals from the supply chain.
- State and municipal institutions in the European Union and of the EU Member States exclude such companies and individuals from public and private tenders.

4. **At the same time,** the European Union and the EU Member States must exert an influence on problematic markets and regimes as a primary task of a coherent foreign, security and development policy to improve the democratic and social development of these countries and strengthen „institution building".

Explanations

By establishing production facilities abroad or purchasing (intermediate) goods produced abroad, globalisation leads to local value creation and prosperity in these countries. In this respect, the protection of human rights, the environment and the prohibition of child labour is prerequisite for modern globalisation.

For many years already, the electrical industry has supported the protection of human rights and the prohibition of child labour by means of the ZVEI Code of Conduct[3]. The protection of human rights and human dignity, good working conditions and no child or forced labour form a self-evident guiding principle for the entire electrical industry.

The commitment of companies to get involved in developing and emerging countries, which is desired by the political sector, would be jeopardised if the integration of these countries in a supply chain/value creation would lead to risks that can scarcely be controlled. The consequence for market participants would be a "quasi-boycott" with counterproductive results in terms of development policy: those who are not active locally cannot be held responsible for human rights violations that exist locally. But those who are not active locally also do not contribute to job creation, local value creation and rising prosperity. This could counteract the principles of local action to fight migration and poverty.

What is the problem?

An industrial company only has a contractual relationship with its direct first supplier and is therefore not contractually bound to most of the suppliers and intermediaries in the background, because it usually buys its components from European wholesalers or component manufacturers. The background suppliers, however, are not subject to EU law according to current legal practice.

But if industrial companies do not have a contractual relationship with these subcontractors and intermediaries, there is therefore also no legal basis and therefore usually no practical possibility of controlling or monitoring them.

Consequently, there is a need to create a legal relationship and the EU stipulations must also apply to non-European suppliers.

N.B.: The only way to make the EU stipulations applicable to non-European suppliers in the supply chain is through a Regulation, not a Directive, because a Directive automatically generates 27 national different stipulations.

[3] Download at www.ZVEI.org

What do we propose as a solution?

Under national and international legal standards and also in view of company workflows, it is possible to stipulate contractual conditions for the production of and trade in primary products in the supply chain. This may include specifications regarding human rights and working conditions as well as explicit prohibitions, e.g. of child and forced labour.

This requires:

1. The stipulation that companies must agree on a binding contractual clause on due diligence compliance with their suppliers, with the inclusion of a passingon clause, i.e. the contractual obligation of the supplier (contracting partner) to pass on these requirements to its suppliers. This results in a chain of contractual stipulations and prohibitions through to the start of the supply chain in non-European countries;

2. The establishment of a European legal framework that also applies to non-European supplier companies

3. A „Human Rights Negative List" created by the EU; and

4. Prosecution of abuses by state bodies.

Details of the proposed solution

This proposed solution is based on existing sanction mechanisms already implemented by European companies because there are already 46 EU sanction regulations that companies are obliged to check and comply with **including sanctions for human rights violations**[4]**.** This regulatory approach can therefore be taken up and optimised without the need to create new mechanisms.

In particular, since 2020 the COUNCIL REGULATION (EU) 2020/1998 of 7 December 2020 concerning restrictive measures against serious human rights violations and **abuses combines the instrument of sanction regulations and lists with abuses of human rights abroad.**

To that end the following division of tasks may apply:

1. Task of state institutions

Primary task of the European Union is the statutory regulation of monitoring measures and the stipulation of an obligation to use a „due diligence clause" and a passing on clause, as well as establishing a European legal framework that also applies to non-European supplier companies.

N.B. 1: Only the state stipulation of a compulsory „due diligence clause" as well as a passing on clause eliminates competition and antitrust concerns about such clauses.

N.B. 2: The only way for continuous control to work in a supply chain is to ensure that not only EU companies are subject to these regulations but also all non-European companies from third countries that have a legal relationship with the EU Single Market.

Secondary task of the European Union is to create a „Human Rights Negative List" with the legal obligation that this must be observed and complied with by all companies, including the prohibition of maintaining business relations with enterprises and individuals stated in the „Human Rights Negative List"[5].

In contrast to companies, state institutions, as a result of their vast organisational structure consisting of ministries, authorities, embassies, general consulates and services, have the means to observe and assess the human rights situation etc. on the ground. The resulting negative findings on violations of human rights etc. are to be recorded in a "Human Rights Negative List".

[4] https://www.consilium.europa.eu/de/policies/sanctions/different-types/

[5] working title, can be amended or optimised at any time

The statutory ruling for a strong protective instrument to safeguard human rights and the environment by the European Union including a „due diligence clause" could have the following wording[6]:

(1) The European Union with the participation of the European Member States creates the necessary lists for monitoring supply chain due diligence and makes them available to both European and non-European companies. These lists follow the legal and administrative requirements of the already existing EU sanction lists and the COUNCIL REGULATION (EU) 2020/1998 of 7 December 2020, for publication in the Official Journal of the European Union. A consolidated full list of the „EU Human Rights Negative List" (working title) will be provided in constantly daily updated form on the websites of the EU.

(2) The European companies are obliged to integrate suitable electronic sanction list tools verifiably in their business processing mechanisms, thus safeguarding compliance.

(3) The supervisory authorities of the European Member States are obliged to monitor the presence of suitable electronic „sanction screening tools". Goods may only be imported into the Community in a supply chain if the use of such monitoring instruments is safeguarded and verified. Monitoring will be carried out by the national customs authorities in the scope of their sovereign tasks in performing customs checks on imports.

(4) As a result of the European Regulation on supply chain due diligence, the companies should integrate the content of the following aspects in their contracts with suppliers:

(a) Deliveries and services (executing the contract) are subject to the contractually binding reservation that internationally recognised human rights, working rights and the protection of the environment are complied with in the extraction, development and production etc. of raw materials, materials and goods and also services.

(b) The contracting partner undertakes not to maintain any business relationship with the companies/individuals stated in the "Human Rights Negative List" published by the relevant legislator. By accepting the contract with the principal, in the capacity of contractor the supplier provides a guarantee in that respect. The contracting partners undertake to furnish all information and documents that are required for any inspection required by the authorities.

(c) In the capacity of contractor, the supplier undertakes to stipulate that subsections 4a and b of the due diligence clause shall be a binding contractual clause for its supplier of goods and services.

(5) Non-European suppliers of European companies respectively suppliers in a supply chain on the EU Single Market are also subject to this European Regulation on supply chain due diligence in order to warrant continuous global protection of human rights and the environment in the supply chains.

(6) Non-European suppliers of European companies respectively suppliers in a supply chain on the EU Single Market who fail to comply with or violate these stipulations and contractual obligations, may be featured in the „EU Human Rights Negative List". Companies featured in the „EU Human Rights Negative List" are excluded from access to the EU market and are prohibited from settling in the territory of the Community. The goods and services of such companies are refused access to the EU market.

[6] test proposal to promote discussion and to show the content and scope of necessary rulings

2. Aufgabe der Unternehmen

The primary task of European companies is to place national and international suppliers under the obligation to take due care in the supply chain by including a „due diligence clause" and a passing on clause in their contracts with their suppliers.

The secondary task of European companies is to observe and comply with the „Human Rights Negative List". This requires the integration of these list entries in the existing EU sanctions modules of corporate compliance tools. Such sanctions modules are required by law.

N.B.: Today already all European companies are obliged to use sanction list tools to observe 46 sanction lists, which also include human rights abuses, and to exclude those in the list as business partners.

3. Consistent behaviour by state institutions and industrial enterprises

Consequences for companies and individuals named in the „Human Rights Negative List" and suppliers who refuse to comply with due diligence obligations could include[7]:

- Companies and their supplier companies exclude companies and individuals named in the „Human Rights Negative List" from the supply chain.
- State and municipal bodies exclude companies and individuals named in the „Human Rights Negative List" from tenders and procurements.
- State and municipal bodies exclude the acquisition of property in real estate and enterprises, also the acquisition of shares, by non-European companies and individuals named in the „Human Rights Negative List."
- State and municipal bodies check and possibly impose immigration restrictions on non-European companies and individuals named in the „Human Rights Negative List."
- In the case of particularly severe violations of human rights, the state and municipal bodies check and possibly impose the freezing of assets of foreign companies and individuals named in the „Human Rights Negative List".
- In the case of severe violations, state bodies possibly prevent market access for goods and services.

[7] These legal consequences and sanctions are already part of the existing European sanction provisions

Why are the approaches to supply chain due diligence currently discussed in the European Union not a viable solution?

1. The approaches to supply chain due diligence currently discussed in the European Union are not linked to already existing EU due diligence regulations

EU Regulation on conflict minerals, timber and diamonds

The existing EU regulations on conflict minerals[8] , timber[9] and diamonds[10] already provide for supply chain due diligence at the European level for certain goods sourced from abroad. These EU regulations already cover some of the **approaches currently discussed in the European Union for supply chain due diligence** as regulation areas already covered by law, so that this would result in duplicate regulation in the EU.

2. The approaches to supply chain due diligence currently discussed in the European Union are also not linked to already existing sanction mechanisms regarding violations of human rights

The COUNCIL REGULATION (EU) 2020/1998 of December 2020 which came into force in December 2020 concerning restrictive measures against serious human rights violations and abuses combines the instrument of sanction regulations and lists with abuses of human rights abroad.

The „Human Rights Negative List" that we propose is prepared by this Regulation and already legitimated by law throughout the EU and part of the EU legal system. **This already existing list now only has to be filled.**

As a supporting and supplementary measure, it should be anchored in law by the EU legislator that all companies that have a legal relationship with the European Single Market are/will be obliged to apply this „Human Rights Negative List" and are/will be obliged to establish and activate corresponding electronic compliance tools.

3. EU Regulation instead of an EU Directive

If the above named EU Regulations on conflict minerals and human rights are not merged with the planned new ruling on supply chain due diligence, similar products and services and identical supply chains will be given different treatment and regulated in multiple fashion (the negative consequences are shown in Annex 1).

Instead of legally dubious duplicate rulings, it would be better if the already existing EU Regulations were merged with the planned new Regulation on supply chain due diligence **into a uniform EU Regulation.**

N.B.: As the above mentioned EU Regulations on certain goods and human rights are Regulations, it would seem counterproductive to have an EU Directive on other due diligence aspects that are partly covered by the requirements of these EU Regulations.

[8] Regulation (EU) 2017/821 of the European Parliament and of the Council of 17 May 2017 laying down supply chain due diligence obligations for Union importers of tin, tantalum and tungsten, their ores, and gold originating from conflict-affected and high-risk areas

[9] Regulation (EU) 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market

[10] Council Regulation (EC) 2368/2002 of 20 December 2002 implementing the Kimberley Process certification scheme for the international trade in rough diamonds

4. „Threshold limit" and small companies

The discussion of **threshold limits**[11] fails to acknowledge that all companies, particularly the large ones, work with long supply chains of considerable depth. The suppliers in these supply chains are often small and mediumsized European companies (SME) with 20 to 500 employees. According to current discussions, they should not be affected by the regulations on supply chain due diligence. However, in view of the fact that these SME are part of the supply chains of the affected companies, the large companies will (have to) force the small ones also to comply and verify supply chain due diligence, as otherwise the due diligence checking chain will collapse and the large company will fail in terms of controls and checking.

The current discussions in the European Union and in some Member States about a threshold limit for due diligence compliance are therefore inappropriate and futile. Instead, the political sector should

- **offer practical, legally binding and workable compliance solutions**
- **give realistic consideration to the concerns of small companies also in their role as suppliers.**

Furthermore, a threshold limit for due diligence compliance should not give the (wrong) impression that smaller companies with less than e.g. 500 employees do not have to comply with human rights in the delivery chain.

A threshold limit is also absurd in argumentative terms, because the meaning of such a threshold limit regarding human rights compliance in the supply chains could lead to the following arguments: **Companies with e.g. 510 employees must heed and comply with human rights in the supply chain. Companies with e.g. 490 employees do NOT have to heed and comply with human rights in the supply chain.**

Our demands for a statutory ruling to warrant continuous, functioning controls in the supply chains:

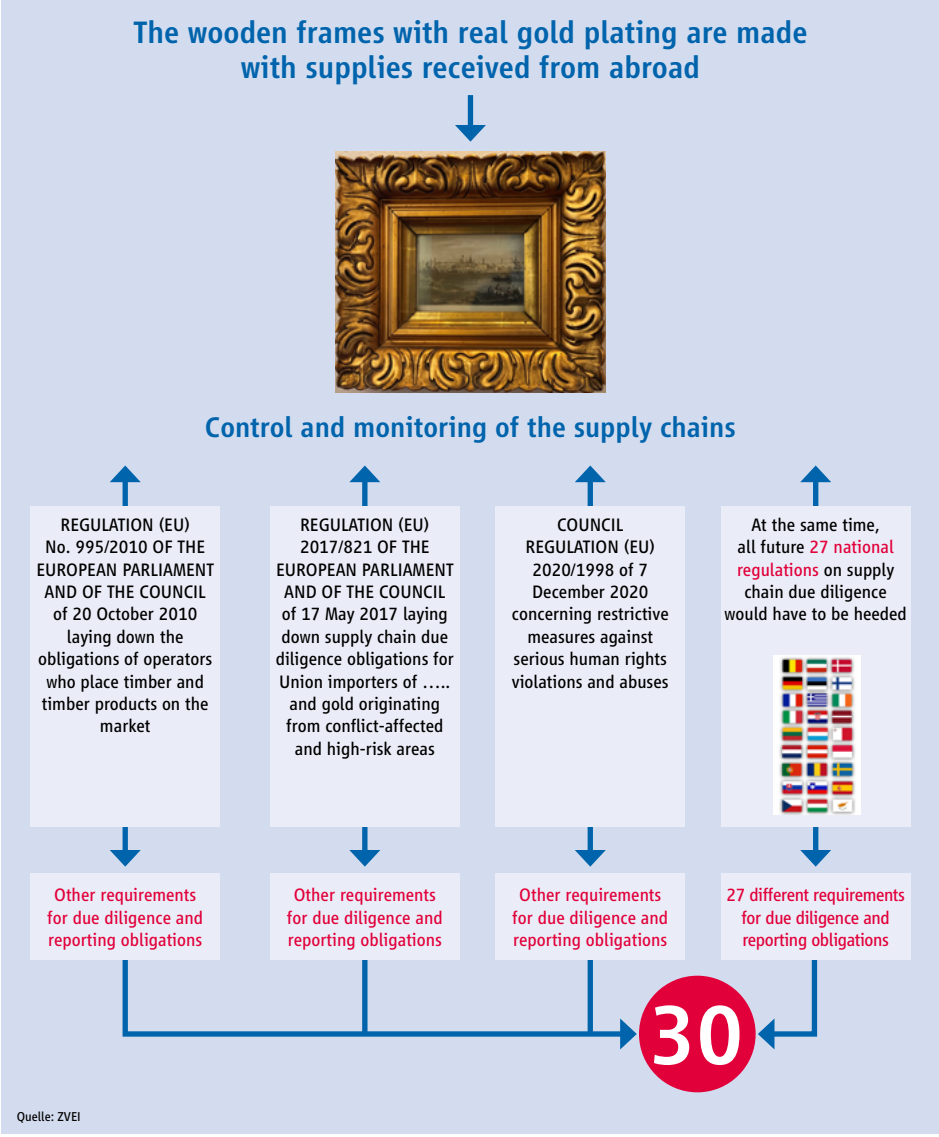
- Practical, legally certain solutions for all sizes of companies
- Registration of companies violating human rights by the bodies of the European Community pursuant to Regulation (EU) 2020/1998
- Obligatory use of a „Human Rights Negative List" as compliance tool in the supply chains
- Every EU company is subject to identical rules by „ONE" EU-Regulation
- Foreign companies are subject to the same rules
- Sanctions in the event of refusal to participate in controls and data collection in the supply chains

[11] „Threshold limits" want to make due diligence compliance dependent on company size

Annex 1 Examples of the usage of different types of legislation

Example 1 for establishing a new EU Directive on supply chain due diligence without merging all already existing due diligence regulations:

A large European group company produces wooden frames with real gold plating in all Member States of the EU with supplies received from abroad.



There is a risk that in manufacturing the same picture frame, the EU company will have to heed 30 different due diligence regulations in identical supply chains.

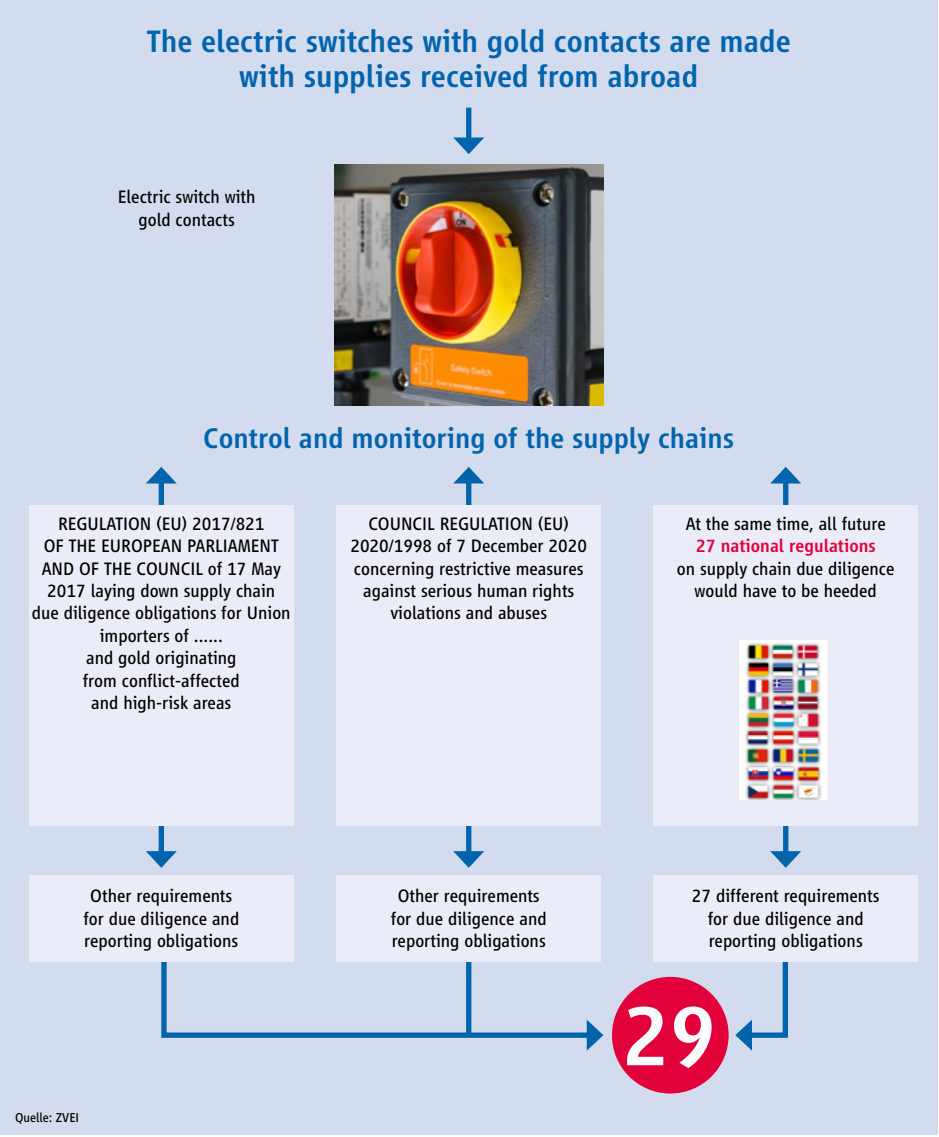
Conclusion: legislative confusion thwarts the protection of human rights through supply chain due diligence.

Remedy: from the legal and entrepreneurial point of view and in its own interests, the EU company feels pushed to pursue the idea of avoiding this legislative confusion by moving its production to a place outside the EU (e.g. in Switzerland) and importing the finished wooden frames in just one EU Member State for distribution throughout the EU.

In terms of turnover, taxation and jobs in the EU this would be a harmful but presumably inevitable consequence.

Example 2 for establishing a new EU Directive on supply chain due diligence without merging all already existing due diligence regulations:

A European large group company produces electric switches with gold contacts[12] in all Member States of the EU with supplies received from abroad.



There is a risk that in manufacturing the same electric switch, the EU company will have to heed 29 different due diligence regulations in identical supply chains.

Conclusion: legislative confusion thwarts the protection of human rights through supply chain due diligence.

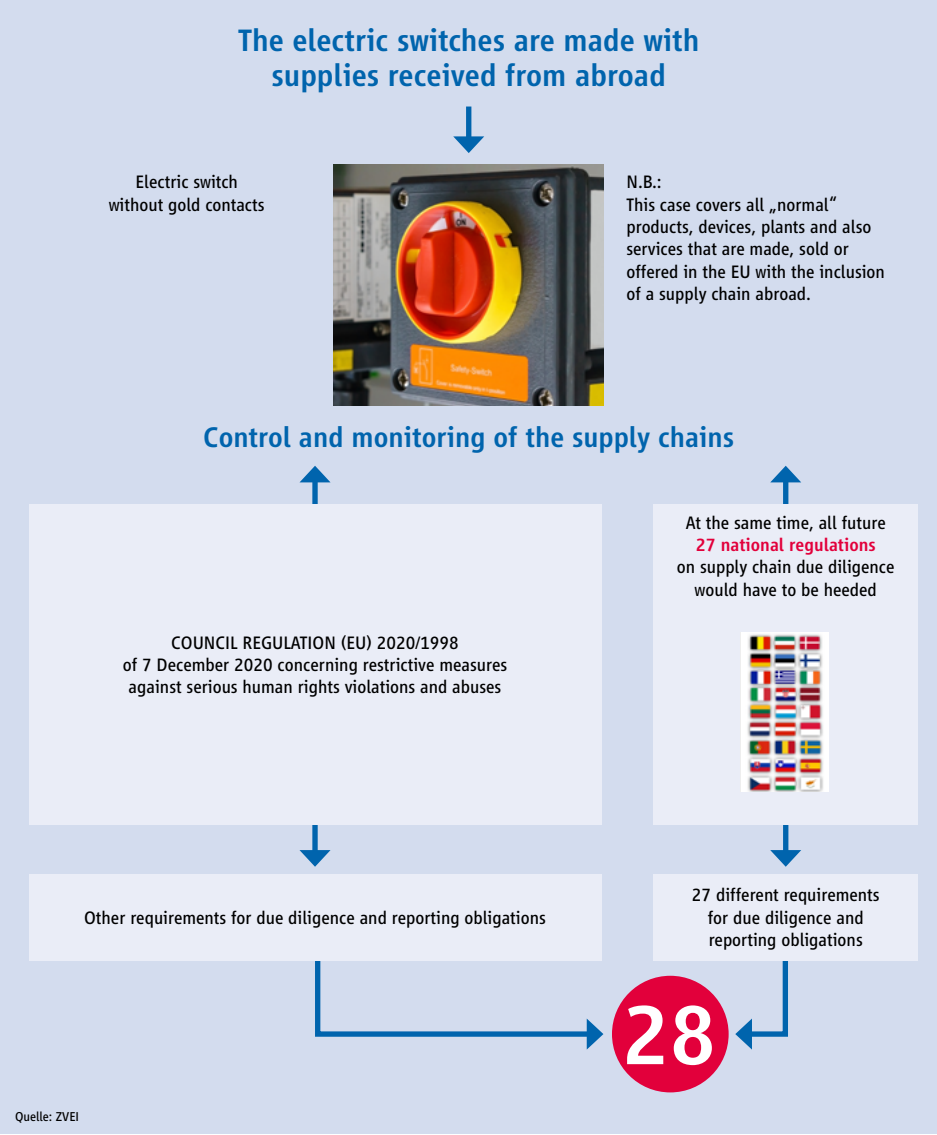
Remedy: from the legal and entrepreneurial point of view and in its own interests, the EU company feels pushed to pursue the idea of avoiding this legislative confusion by moving its production to a place outside the EU (e.g. in Switzerland) and importing the finished electrical switches in just one EU Member State for distribution throughout the EU.

In terms of turnover, taxation and jobs in the EU this would be a harmful but presumably inevitable consequence.

[12] Gold coatings are used in devices/components/machinery/plants/vehicles/IT/communication/aerospace technology/e-Mobility/digitalisation, etc. to avoid corrosion and the loss of contacts

Example 3 for establishing a new EU Directive on supply chain due diligence without merging all already existing due diligence regulations:

A European large group company produces electric switches (without gold contacts) in all Member States of the EU with supplies received from abroad.



There is a risk that in manufacturing for import or production of all products and services, the EU company will have to heed 28 different due diligence regulations in identical supply chains.

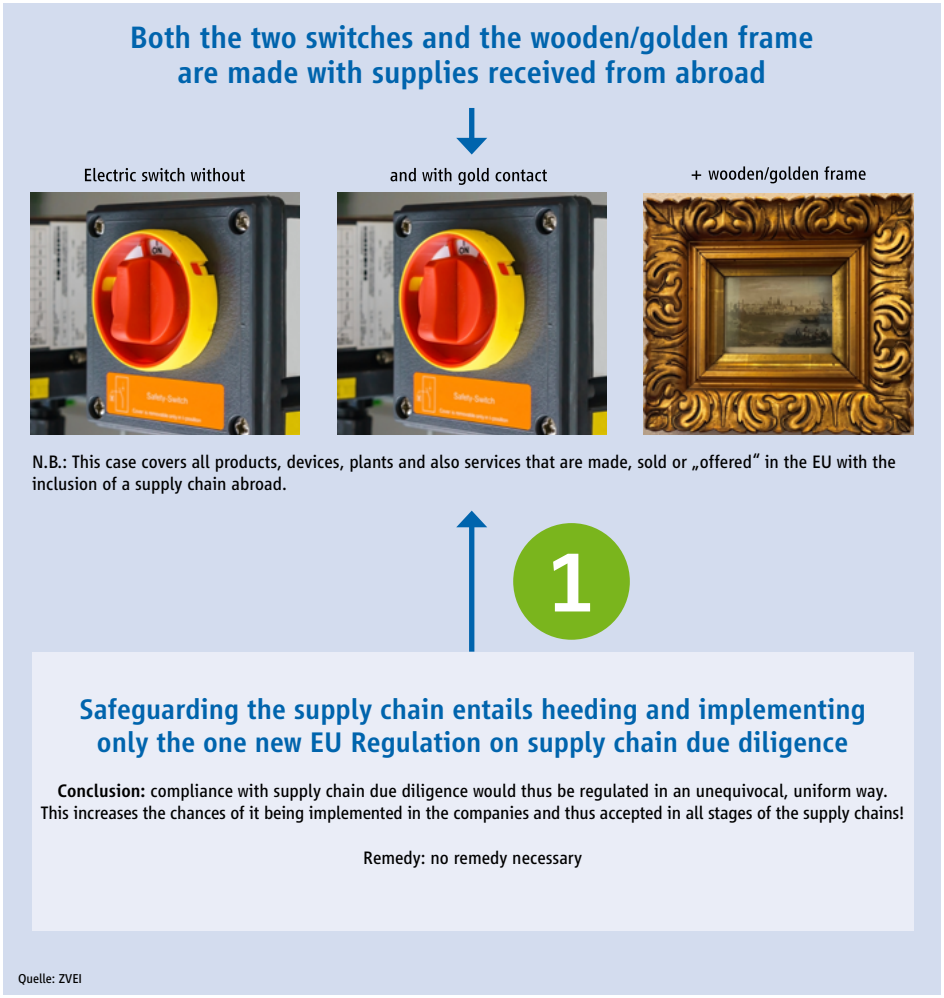
Conclusion: legislative confusion thwarts the protection of human rights through supply chain due diligence.

Remedy: from the legal and entrepreneurial point of view and in its own interests, the EU company feels pushed to pursue the idea of avoiding this legislative confusion by moving its production to a place outside the EU (e.g. in Switzerland) and importing the finished electrical switches in just one EU Member State for distribution throughout the EU.

In terms of turnover, taxation and jobs in the EU this would be a harmful but presumable inevitable consequence.

Example 4 for establishing a new EU Regulation on supply chain due diligence with the merger of all already existing due diligence Regulations:

An electric switch is delivered with and without gold contacts respectively a wooden/golden frame is manufactured.



Example 4 shows:

1. what is realistically feasible. Controlling and safeguarding the supply chains can only be implemented by ONE clear statutory requirement, if at all.
2. that if the legislator really wants to play an active role in protecting human rights, ONE regulation has to be created that can be heeded and implemented in uniform fashion by all EU companies.
3. that the current development by which EU companies have to heed up to 30 regulations for the same product and the same supply chain is unacceptable; as a result, this situation means that despite making every effort, no company can implement this kind of legal confusion.
4. that it is possible to avoid excessive bureaucracy with high costs.
5. that it is possible to avoid the danger of supply chains, trade flows, production facilities and branch sites from being moved abroad.

We ask the legislator to establish only this clear, legally certain version No. 4, i.e. to pool all due diligence requirements in one EU Regulation!

Annex 2 How a „Human Rights Negative List“ works

Depiction of how a „Human Rights Negative List“ can be used to protect human rights in supply chains and how it would work

Instrument for controlling and warranting compliance with human rights

Practical instruments that can be used with legal certainty in companies of all sizes are needed to make it possible to protect human rights in supply chains. Simply making it compulsory by law for companies to comply with vague supply chain due diligence is certainly insufficient. What is necessary is for the state, society and the companies to work together on an expedient solution.

A corresponding division of labour would entail the state (EU Member States and the Commission through their secret services, administrations, embassies and general consulates) issuing a binding „Human Rights Negative List“, with the business companies ensuring that this list is integrated in their existing sanction list tools, with corresponding reviews being carried out accordingly.

Sanction lists for safeguarding human rights

The instrument of the EU sanction lists can easily be used also for monitoring violation of human rights by governments, individuals or companies. The lists can also be extended to include violations of occupational safety provisions and environmental damage.

This proposed solution is based on existing sanction mechanisms already implemented by European companies, because there are already 46 EU sanctions regulations that companies are obliged to examine and comply with, **also already including sanctions for human rights violations (available at: https://www.consilium.europa.eu/de/policies/sanctions/different types).**

In particular, with the **COUNCIL REGULATION (EU) 2020/1998 of 7 December 2020 concerning restrictive measures against serious human rights violations and abuses,** the EU has activated the instruments of sanction controls for safeguarding human rights and for prosecuting abuses against human rights.

This regulatory approach can therefore be taken up and optimised to protect human rights without the need to create new mechanisms.

What are the EU sanction lists?

The EU sanction lists name legal entities (companies, organisations) and individuals who are to be ostracised for breaching international law, violating human rights, terror activities or infringing political standards.

> The statutory provisions for sanction screening can be found on the one hand in the Terrorism Regulation (COUNCIL REGULATION (EC) 2580/2001of 27 December 2001 on specific restrictive measures directed against certain persons and entities with a view to combating terrorism)
> and on the other hand in nearly all European embargo regulations, such as for example the Russia Embargo (COUNCIL REGULATION (EU) No 833/2014 of 31 July 2014 concerning restrictive measures in view of Russia‘s actions destabilising the situation in Ukraine),
> the Iran Embargo (COUNCIL REGULATION (EU) No 267/2012 of 23 March 2012 concerning restrictive measures against Iran and Repealing Regulation (EU) No 961/2010)
> together with 44 other regulations that are constantly being expanded.

Is compliance with sanction lists compulsory?

According to the regulations on sanction screening (also known as sanction list control, business partner control, business screening, business partner screening), it is compulsory by law for every company to review every business deal or business transaction with individuals, organisations or companies to ascertain that the business partners, companies or organisations are not on the European sanction lists. **If they are, then the business is prohibited.**

Who has to heed sanction lists?

Without any exceptions, it is strictly forbidden (prohibition) for all EU legal entities and individuals to pursue business with the legal entities (companies, organisations) and individuals named in the EU sanction lists.

How are sanction lists checked?

Companies usually check sanction lists with an electronic software tool that checks the business partners regularly on the basis of sanction lists that are updated on a daily basis. The tool triggers an alarm on recognising a business partner as being listed.

Frequently asked questions (FAQs)

1. Can an entrepreneur say: „I didn't know that my business partner is on the sanction list"?

No, this simple excuse won't work because everyone is obliged to proceed with sanction list checks. Nor can this excuse be „generated" by not conducting any sanction list checks in the company or as an entrepreneur (along the lines of "I can't discover what I don't check"), because this kind of failure to proceed with sanction checks constitutes negligent behaviour that breaks the law.

2. Can something happen to me if I ignore the sanction regulations and do nothing (no checks)?

Yes, the failure to proceed with sanction list checks constitutes active violation of the existing law.

3. Can this check be carried out by third parties?

Yes, in particular small companies or companies with no experience with such procedures may arrange for sanction screening to be carried out by third parties with verified expertise.

4. Does the use of a sanction list to check compliance with human rights in the supply chain generate legal certainty?

Yes. In view of the fact that it is the task of the European legislator to list all legal entities and individuals violating human rights, the company acts with legal certainty when it checks the sanction lists and does not allow any business with listed persons.

5. Is legal certainty generated by the simple legal obligation to safeguard compliance with human rights in the supply chain (without the compliance tool suggested by us) e.g. with a due diligence law?

No, because in this case, the legislator simply transfers its responsibility for protecting human rights to the companies without providing practical, legally certain implementation instruments. When a legislator evades responsibility in this way, it not only causes legal uncertainty on the part of the companies but may have even more serious consequences such as potential criminalisation.

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