

SUPPLY CHAIN ACT

Why these medium-sized companies want more regulation

In an open letter, entrepreneurs criticize the “misapplication” of the Supply Chain Act – and defend the EU law. What is on their minds.

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Munich Electrification is in favor of the EU Supply Chain Law. The medium-sized company builds battery management systems, for Daimler Truck among others. Photo: Munich Electrification GmbH

For Isabel Palacios, it is about fundamental values: she believes that strengthening human rights and environmental protection makes sense. That is why the sustainability officer supports the Supply Chain Act. So much for the theory.

In practice, however, full transparency in the supply chain sometimes seems like an impossible task. Palacios works for Munich Electrification, a medium-sized manufacturer of battery components. With 230 employees, Palacios' employer does not fall under the German supply chain law, as it is too small. But her customers, including major automotive brands, are subject to it – and they are demanding more and more details.

Palacios doesn't have an answer for every question. "Often, contracts and questionnaires contain clauses or requirements that are currently almost impossible for us to fulfil in practice," she says. It is also because of such consequences that the Supply Chain Act is, for many small and medium-sized companies in Germany, above all a bureaucratic burden.

Many associations are therefore calling for it to be scrapped. They are praising the initiative of the EU Commission, which announced at the end of February that it would be weakening and postponing a number of sustainability laws. These include the European Supply Chain Act.

But Palacios and her employer have come to a different conclusion: together with 14 other medium-sized companies, Munich Electrification is reaching out to the public and advocating for a supply chain law at the EU level.

In the statement, which WirtschaftsWoche has seen, the companies call for the swift implementation of the EU Supply Chain Law and concrete relief for small and medium-sized enterprises (SMEs). Most of the practical problems result not from the German Supply Chain Law itself, the signatories argue, but "from an inadequate or simply incorrect application of the law.

SMEs criticize the fact that large companies pass on their obligations to small and medium-sized companies. However, small and medium-sized companies in particular often lack the knowledge to be able to assess what their actual obligations are as companies that are not directly covered by the supply chain law.

The 15 supporters of the statement come largely from the manufacturing industry. They include family businesses such as Richard Henkel (steel tube furniture and surface technology) and Oskar Pahlke (foam), as well as young medium-sized companies such as the smartphone manufacturer Shift. Other signatories include the Geiger Group (plastics technology) and Jöst Abrasives (abrasives). They all have in common that they are not themselves subject to the law, but as suppliers they are indirectly affected by it.

Stefan Prakesch supports the statement and is the managing director of Aris, a manufacturer of rainwater harvesting systems. He says: "To understand debureaucratisation as the dismantling of fundamental human rights and environmental standards, of all things, is a pitiful understanding of entrepreneurship." Instead, there are many other measures that would relieve the burden on SMEs but not harm anyone – for example, in VAT law.

NO SHIFTING OF OBLIGATIONS TO SUPPLIERS

The companies are calling on the German government to integrate the planned EU Supply Chain Directive (CSDDD) into the German Supply Chain Act (LkSG) as quickly as possible. They consider a European solution to be sensible in order to guarantee a level playing field. However, instead of the announced postponement and renegotiation, they would like to see planning security.

They are also calling for an effective ban on the transfer of obligations to suppliers. Large companies are obliged to exercise due diligence in their supply chains under the Supply Chain Act. They are required to carry out a risk analysis in order to obtain more precise information from specific points in the supply chain.

This makes it clear that blanket questionnaires sent to all suppliers or passing on the due diligence obligations through contractual clauses are not in line with the law. The Federal Office for Economic Affairs and Export Control (BAFA), which is responsible for this area, has already made it clear in several handouts that the LkSG obligations may not be passed on. However, the signatories criticize that this warning has “so far had little practical effect”.

Isabel Palacios from Munich Electrification knows this from her own experience. Her company's battery components contain small amounts of certain conflict minerals. “Since there is no absolute transparency regarding the mining of the minerals, we cannot sign a declaration that there are no human rights violations in the upstream supply chain,” explains Palacios. She always tries to explain this to customers. However, other SMEs may sign the clauses for fear of being disadvantaged when it comes to awarding contracts.

“For many small and medium-sized companies, the way the Supply Chain Act has been implemented in Germany so far is a cause for concern,” says signatory Christian Göbbert, Chief Research & Science Officer at Nanostone Water, a manufacturer of ceramic filters. Nevertheless, he says, the company ‘supports the goals and values of the law’.

Both BAFA and the association “Der Mittelstand. BVMW” confirm the statement that many large companies pass on their obligations and overwhelm SME suppliers with undifferentiated queries. A BAFA spokesperson confirmed that an unlawful approach to suppliers can lead to sanctions such as penalty payments, warnings, fines or the exclusion of a company from public procurement.

BAFA has now set up a reporting office for this reason. So far, the agency has received “a double-digit number of reports of attempts to shift obligations or a non-risk-based, inappropriate approach to suppliers”. The agency has not yet imposed any sanctions.

At Munich Electrification, Isabel Palacios and two other colleagues are voluntarily taking care of sustainability in the supply chain. They don't use external consultants, but instead attend many seminars, for example, from the German government's Helpdesk for Business and Human Rights.

But is all this effort really necessary? Palacios is convinced that her work will pay off in the medium term. After all, a more transparent supply chain is more resilient. “In my contact with our own suppliers, I can see that supply chains are already more transparent than they were a few years ago,” says Palacios. She hopes that more companies will join the call.