



ESG in Germany

Drs Friedrich Gebert, Andrea Panzer-Heemeier and Mirjam Boche give an overview of ESG requirements in the German market

I. COUNTRY INSIDE – ESG INNOVATIONS AND LATEST REQUIREMENTS IN GERMANY

When it comes to new trends and standards for companies, three letters are on everyone's mind: E, S and G. ESG is increasingly evolving from a marketing buzzword to a core figure that now has a significant impact on the business model of each company. In Germany, ESG requirements are becoming more and more binding and standardised. Therefore, ESG regulations have recently changed significantly. Whether on an environmental, social or governance level, both the EU and especially German lawmakers are getting serious about moving towards a sustainable economy. Through the EU Green Deal, the EU has set itself the goal of transforming the European economy

Allowances (EUAs), for each tonne of CO₂ they emit. Companies can use carbon offsets, called Certified Emission Reductions (CERs), to meet part of their emissions reduction targets. The EU ETS aims to limit emissions and therefore is based on a 'cap and trade' principle in which only a limited number of EUAs is made available. The number of EUAs is reduced over time so that total emissions decrease.

In April 2023, the EU Parliament adopted a reform of its EU ETS. Climate protection regulations keep getting tighter and more industry sectors are included in the regulatory schemes. As key points, the reform includes stricter requirements for installations already subject to the EU ETS (ETS I), the gradual inclusion of maritime transport in ETS I

postpone the start until 2028. Not all details have been worked out yet, especially as member states are allowed to exempt fuel suppliers from the EU ETS II in case a national carbon price scheme with a price level equivalent or higher than the EU system exists.

German and European lawmakers will also introduce a Carbon Border Adjustment Mechanism (CBAM), which will be fully operational in 2026. As part of the Fitfor55 legislation, the EU Commission has introduced a climate tariff. With the CBAM the EU is imposing its own CO₂ price on third countries and therefore de facto extends the EU ETS to the world. Under the CBAM, products imported into the EU will be charged a price that corresponds to the price of the EUAs. Companies wishing to sell in the EU have to buy CBAM allowances from national authorities and thus pay the EU CO₂ price, regardless of where in the world they produced. This will make production outside the EU with a lower/no CO₂ price less attractive. The price of CBAM allowances will only fall to the extent that the product was already subject to a CO₂ price outside the EU. The sectors initially affected are cement, steel, aluminium, fertilisers, and electricity, as well as the first processing stage. The new CO₂ border adjustment is a powerful climate policy tool. Importers who do not have enough CBAM allowances will be fined €100 per missing allowance.

'The EU has set itself the goal of transforming the European economy and making it sustainable. To achieve this goal, the EU is using all the instruments at its disposal and is currently initiating major regulatory projects in many areas.'

and making it sustainable. To achieve this goal, the EU is using all the instruments at its disposal and is currently initiating major regulatory projects in many areas.

This article outlines the key ESG innovations and recent developments in Germany that companies should have on their radar in 2023. These include whistleblower protection, the European emissions trading and carbon adjustment mechanism, new regulations on forever chemicals, the supply chain management, and new ESG reporting obligations.

1. Emissions trading system and carbon border adjustment mechanism

In Germany and Europe, the use of carbon offsets to meet net zero or carbon neutral commitments is currently primarily regulated by the EU Emissions Trading System (EU ETS). Under the EU ETS, companies in sectors such as power generation and heavy industry must hold permits, called European Union

from 2024 and a new emissions trading system (ETS II) for buildings, road transport and additional sectors.

The extension of the EU ETS I to maritime activities means that shipping companies will also be required to surrender several EUAs equal to their total emissions in the previous calendar year by the end of September each year. As a result, shipping companies will be required to monitor and report their emissions, and to purchase and surrender EUAs accordingly. The renewal of ETS I shall apply from January 2024. Therefore, shipping companies are required to be prepared to ensure compliance with the regime and avoid facing severe penalties.

Additionally, a separate emission trading system will be introduced for emissions currently not priced across the entire EU. EU ETS II will include emissions from the building sector as well as from road transport and the usage of fuels in other, as of now not defined, sectors. The EU ETS II will become operational from 2027 onwards, while high energy prices may even

2. Whistleblower protection in the EU and in Germany

From 2023 onwards, the new EU Whistleblowing Directive and the German 'Hinweisgeberschutzgesetz' will require companies to introduce a new whistleblowing system (WBS). The new law applies to companies with over 250 employees (starting 17 December 2023: over 50 employees). The law requires for whistleblowers to provide information in oral or written form. At the whistleblower's request, a personal meeting with the whistleblower must also be possible. Companies are obliged to always respect the confidentiality of the whistleblower and all third parties mentioned in each reporting. The law sets clear deadlines for processing the information. For example, the whistleblower must receive an acknowledgement of receipt within seven days. After approximately three to four months, feedback on the processing status must be provided. During processing,



Dr Friedrich Gebert

‘There has been a great deal of uncertainty about the rules governing ESG reporting and the various international standards and certificates in place. The risk of greenwashing is considered to be high.’

companies are required to ensure that the information is received and processed by an impartial person or department within the company. The WBS can also be integrated into an existing compliance management system. Legal requirements must be met both during the implementation and operation of the WBS, including data protection and employee participation.

3. Forever chemicals

Another environmental issue relates to a chemical topic that will become increasingly important in the next years and will cause significant disruption in the affected industries: forever chemicals such as Perfluoroalkyl and Polyfluoroalkyl Substances (PFAS). PFAS have been a topic of increasing concern in Germany due to their persistence, bioaccumulation, and potential health and environmental impacts. In recent years, German authorities have taken various measures to address PFAS contamination and exposure. For example, the German Environment Agency (Umweltbundesamt) has published a report recommending stricter regulations on PFAS, including a ban on non-essential uses of PFAS and tighter controls on industrial releases of the chemicals. In addition, the German Federal Ministry for the Environment, Nature Conservation, Nuclear Safety and Consumer Protection (Bundesministerium für Umwelt, Naturschutz, nukleare Sicherheit und

Verbraucherschutz) has launched a national action plan to reduce PFAS contamination, which includes measures such as monitoring and testing of drinking water, soil, and food, as well as research on alternative chemicals and technologies.

Most recently in January 2023, Germany submitted a request to the EU’s chemicals agency, ECHA, to ban PFAS forever.

4. Supply chain management

The focus of national and European legislation in recent years has also been more and more on human rights standards along the supply chain. The German ‘Lieferkettensorgfaltspflichtengesetz’ (LkSG) now requires companies with over 3,000 employees (starting 2024: over 1,000 employees) to take measures to prevent human rights violations and environmental harm in their supply chains, for example child or forced labour. This includes conducting regular due diligence assessments of their suppliers and taking appropriate remedial actions where necessary. Companies are also required to establish complaint mechanisms for employees and other stakeholders to report potential violations of human rights or environmental standards in their supply chains. Failure to comply with the LkSG can result in fines and reputational damage for the companies.

On the European level, a new supply chain law is in the making as well, the European

Corporate Sustainability Due Diligence Directive (CSDDD). The Commission’s proposal sets out stricter due diligence requirements for companies in the EU. Companies will soon have to ensure that child labour, slavery, labour exploitation, pollution, environmental degradation, and biodiversity loss do not occur in their supply chain. In addition, certain companies will have to establish a plan to ensure that their business strategy is compatible with limiting global warming to 1.5°C in accordance with the Paris Climate Agreement. While the Commission’s proposal applied to companies with 500 or more employees, the European Parliament tightened the proposal again on 1 June 2023. The scope of application now will start at 250 employees. The EU triologue procedure is underway, a precise timetable has not yet been set, but companies with business in Germany and the EU should closely monitor the CSDDD development.

5. ESG reporting obligations

In 2023, ESG reporting obligations are on the radar of most companies. There are various ESG reporting requirements in place to monitor compliance with ESG regulations and to help companies to further promote themselves. However, there has been a great deal of uncertainty about the rules governing ESG reporting and the various international standards and certificates in place. The risk of greenwashing is considered to be high.



Dr Andrea Panzer-Heemeier

‘Regulators, customers, employees and investors all increasingly expect credible ESG programmes with measurable objectives.’

Some ESG reporting requirements have been in place since 2017, notably through the Non-Financial Reporting Directive (NFRD). But now, in January 2023, the game changing Corporate Sustainability Reporting Directive (CSRD) entered into force. This new directive modernises and strengthens the rules about the social and environmental information that companies are obliged to report. A broader range of companies are now required to report on sustainability – around 50,000 companies in total. The new rules will ensure that investors and other stakeholders have access to the information they need to assess investment risks arising from climate change and other sustainability issues. The directive will also create a culture of transparency about the impact of companies on people and the environment. Finally, reporting costs will be reduced for companies over the medium to long term by harmonising the information to be provided. Companies will have to apply the new rules for the first time for the financial year 2024. Companies subject to the CSRD will have to report according to European Sustainability Reporting Standards (ESRS). The Commission is expected to adopt the first set of standards by mid-2023.

The EU has also established the Sustainable Finance Disclosure Regulation (SFDR), which requires financial market participants to disclose information on the sustainability of their investments. This regulation aims to prevent greenwashing in the financial sector by ensuring that investors have access to reliable and comparable information on the environmental and social impacts of investment products. In Germany, in addition to implementing the European reporting directives companies must also comply with the ESG reporting requirements of the LkSG. The LkSG requires companies to report on how they identify human rights risks and environmental issues as well as how they intend to minimise these risks and comply with their due diligence obligations.

II. ESG THE ARQIS WAY: MAKE BUSINESS POSITIVE

Regulators, customers, employees and investors all increasingly expect credible ESG programmes with measurable objectives. Companies that fully exploit the potential associated with sustainability commit to a lasting sustainability management. A targeted

transformation process has to be embraced by all company departments and divisions. Sustainability must be accepted as an essential corporate value, integrated in the operational strategy and managed by way of clear communication.

At ARQIS, these ESG topics are not just another label for legal advice already conventionally provided. Our integrated consulting concept covers all the relevant fields of law, offering structured advice on all important aspects of sustainability and ESG. We truly believe that value-driven management and leadership is the key to sustainable success and implement these principles in our own corporate culture. For example, ARQIS is ‘NetZero’ since 2020. We obtained a very detailed picture of our own carbon footprint. We are certified as a climate-neutral company. However, we are aware that we have to focus on the continuous reduction of our carbon footprint going forward. The ARQIS GreenTeam brings together many of our law firm’s employees, who have been tasked with designing and developing minor and major improvements that will continuously reduce our footprint. ARQIS continues to profile itself as a diverse and ‘people and purpose centric law firm’. Well-known clients such as Volkswagen, Delivery Hero, Omnes, Sunfire and state-owned energy companies including large municipal utilities rely on us when it comes to legal and ESG issues.

We have special expertise in:

- **Circular economy.** A European circular economy is a huge opportunity for the economy, the environment, and the climate. At the same time, it is an immense challenge for the industry. We help you meet the new legal requirements, such as for packaging or the fashion industry.
- **Hydrogen economy.** The energy and transport revolution will not succeed without hydrogen. Green hydrogen is expected to replace coal, oil and gas in the future. We have been supporting our clients across the hydrogen value chain since the start of the hydrogen revolution.
- **Energy and transport transition.** The energy and transport transition will change everything. The risk of ESG-related litigation is increasing. We keep an eye on upcoming and existing obligations and create solutions tailored to your business.
- **Decarbonisation.** The regulatory requirements for decarbonisation are enormous. The legislator has set national climate protection. We can help you

‘We are certified as a climate-neutral company. However, we are aware that we have to focus on the continuous reduction of our carbon footprint going forward.’



Dr Mirjam Boche

prepare for, comply with and implement these new regulatory requirements.

- **Company reports.** From a regulatory perspective, corporate reporting already plays an important role in the context of ESG. It is not only necessary to report on how sustainability risks affect the company, but also how the company's activities affect sustainability issues.
- **ESG supply chain management.** The German LkSG requires companies to comply with human rights and environmental standards in their supply chain. We help companies to meet this new set of regulations.
- **Remuneration.** Advising on and designing remuneration models is a key focus of our HR.law team.
- **Diversity/anti-discrimination.** Making diversity and inclusion a reality at all stages of working life is a focus of our consultancy.
- **Workplace and corporate co-determination.** Our team has many years of experience and extensive expertise in both workplace and corporate co-determination.
- **Data protection.** The increasing importance of digital work and the

associated collection and processing of data, including increasingly stringent requirements and sanctions, is reason enough for us to have a dedicated team to advise on all aspects of digital data.

- **Whistleblower protection and risk management.** The imminent introduction of the obligation to implement a whistleblowing system creates a need for action for most companies.
- **M&A transactions.** We understand the importance of ESG matters for potential investors, in particular in the private equity sector, and specifically address these in our M&A-related advice.
- **Manager liability and corporate governance.** Management liability and corporate governance challenges are key areas of our expertise. In particular, we are familiar with the specific requirements of listed companies and assist our clients in observing capital market related compliance requirements such as insider regulations.
- **Compliance and risk management.** We support you with the conceptual design and effective implementation of a comprehensive and ESG integrated compliance management system.

ARQIS
ARQIS Rechtsanwälte
Partnerschaftsgesellschaft mbB
Breite Straße 28
40213 Düsseldorf

E – Environmental:
Dr Friedrich Gebert
T: +49 211 13069 2076
F: +49 211 13069 099
M: +49 173 430 0328
E: friedrich.gebert@arqis.com

S – Social:
Dr Andrea Panzer-Heemeier
T: +49 211 13069-145
F: +49 211 13069-099
M: +49 173 7291 414
E: andrea.panzer-heemeier@arqis.com

G – Governance:
Dr Mirjam Boche
T: +49 211 13069 291
F: +49 211 13069 099
M: +49 173 7291 409
E: mirjam.boche@arqis.com

www.arqis.com/en