

# Rödl & Partner

NEWSLETTER LATVIA

SETTING ACCENTS

Issue:  
June 2022

Supply-chain compliance and due diligence in Latvia

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## → Supply-chain compliance and due diligence in Latvia

The concept of supply-chain transparency and its due diligence is rather novel. Yet today it commands minds of nearly all managers of the companies around the globe. Companies are under pressure from governments, customers and other stakeholders to obtain more information about their supply-chains and just the reputational cost of failing to do so may be high.

Besides, studies show that customers may be willing to pay 2 to 10 per cent (some of the researchers refer to even higher values) more for products from companies that provide greater their supply-chain transparency. Therefore supply-chain compliance and due diligence takes its permanent and increasing role in each and every business gaining immediate value in the eyes of your investors, lenders and purchasers.

### EU legal framework as a set of minimum requirements

On 23 February 2022, the European Commission adopted a proposal for a Directive on corporate sustainability due diligence thus expanding the EU common rules on corporate sustainability. First of all, the new Directive must be looked at by observing that there is already a number of EU legislative acts, which tackle sustainability issues, for example:

- Non-financial Reporting Directive, 2014 (NFRD);
- Sustainable Finance Disclosures Regulation (SFDR), 2019;
- Taxonomy Regulation, 2020;
- European Climate Law, 2021.

Second, the proposal for this Directive aims to foster sustainable and responsible corporate behaviour. It applies to the company's own operations, their subsidiaries and their value chains (direct and indirect business relationships). The companies will be required to identify and, where necessary, prevent, end or mitigate adverse impacts of their activities on human rights and on the environment. Among other, the proposed consequences are to impose an obligation to cease all the business relationships, which, for example, might contribute to the exploitation of workers or pollution, or biodiversity loss. In addition, the proposal makes all companies in scope liable for failure to comply with due diligence obligations.

In addition, an important aspect of the draft is expanding the concept of parent company liability. Namely, the parent companies in EU will be liable for the corporate due diligence violations committed by their daughter companies anywhere on the globe.

### General obligations on supply-chain analysis in Latvia

"Know Your Business Partner", both towards the supply and delivery side, itself is a relatively new corporate concept. In its core there is an obligation to manage the company's business partners relationship and their associated risks to ensure that the company does not contribute to the tax evasion, money laundering, to the wealth of the subjects under the sanctions or similar. Such obligations are mandatory for any company regardless of its size, industry, turnover or any other criterion.

The general supply-chain investigation standard in Latvia does not go beyond the minimum set of requirements as adopted by the EU institutions, except some specific additional requirements in preventing money laundering and the applicability of external sanctions regimes, such as the USA OFAC sanctions. Subsequently, the companies originating from Latvia will usually have more detailed internal processes on the above listed topics. And, on the contrary, the foreign companies entering the Latvian market must pay an additional attention to these issues to ensure the full compliance.

As regards sustainability impact analysis and related reporting requirements then there are no country specific rules. In particular, NFRD serves as the core for the mandatory reporting content and requirements. The most often used non-financial information reporting standard is UN Global Compact, GRI or more and more popularity gaining Nasdaq ESG Reporting Guide.

There are companies, which voluntarily assume sustainability reporting practice. In most cases the main driver for such a decision is using the reporting standard as a basis for a systemic approach on corporate sustainability issues.

## Supply-chain sustainability risk analysis as a part of corporate governance

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On December 2020 the Corporate Governance Code (hereinafter – the Code) was adopted in Latvia, which provides the good corporate governance recommendations for the locally operating companies. The Code is based on the G20/OECD *Principles of Corporate Governance (2015)*. As the soft law instrument the Code is not binding.

However, since the public discussions on the importance of corporate governance, including its link to a company's financial performance in the medium and long term, during the period of the Code's preparation, the awareness of Latvian companies on these issues has grown significantly. It is also worth noting that lenders, especially banks, are taking a closer look at the corporate governance model of companies.

Among the key principles of corporate governance, such as the development of a corporate strategy, the establishment of an internal culture and a Code of Conduct, appropriate internal and external control systems, etc., the Code also includes guidance on risk management and the need for appropriate legal risk management policies. The Counterparty Research Policy is one of the three legal compliance policies recommended by the Code, alongside the Personal Data Processing Policy and the Sanctions Risk Management Policy. Although

the Code does not specifically address the necessity for a supply-chain risk analysis, it is an essential part of counterparty due diligence. One of the tools increasingly used for supply-chain risk management in Latvia is the development and application of company-specific Supplier Code of Conduct. These codes of conduct usually include not only the minimum requirements of the draft Directive on due diligence in the field of corporate sustainability, but also other conditions for the cooperation with the company, such as the requirement for the business partner to ensure non-discrimination of its employees, decent working conditions, protection of personal data, etc.

As of 19 March 2022, Latvia is required to comply with the principles of the Code in both wholly and partly state-owned companies. Accordingly, these companies are now obliged to carry out supply-chain due diligence and to implement appropriate sustainability measures when collaborating with their business partners. However, when planning deliveries to business partners in Latvia, it is important that companies in Germany and other countries know that the local business partner, a state-owned company, will carry out a supply-chain due diligence, whereas other companies can currently do so at their own discretion. Despite this voluntary principle, the intangible qualities of a business partner, such as reputation, are of increasing importance in Latvia.

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