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UNICE

Union des Confédérations de l'Industrie et des Employeurs d'Europe
Union of Industrial and Employers' Confederations of Europe

GUIDELINES FOR PARTNERSHIP

IN INDUSTRIAL SUBCONTRACTING

EUROPEAN COMMISSION
Directorate-General XXIII: Enterprise Policy, Distributive Trades, Tourism and Cooperatives

A UNICE-DG XXIII initiative

Mr François PERIGOT ⇨ **(photo+signature)**

President of UNICE, Union of Industrial and Employeurs' Confederations of Europe

UNICE, in collaboration with the European Commission, is pleased to publish this guide, which proposes ground rules and principles that have proved their worth for building solid and dynamic partnerships in subcontracting. This guide is based on the best practice identified, in particular, in the areas of payment conditions, quality, industrial property and specialised cooperation arrangements.

Because it brings together the great majority of firms of all sizes (large, medium and small), UNICE could not ignore the economic relations between these partners, who tend to be too often considered in isolation even though their fates are closely linked. The prosperity of SMEs is dependent on the success of their larger customers and, conversely, the competitiveness of large companies depends in large measure on the quality of the work supplied by small and medium-sized enterprises.

UNICE is convinced that exercise of a certain amount of self-regulation by all parties is the best approach for injecting dynamism into subcontracting relationships, in the interests of all concerned.

Mr Christos PAPOUTSIS ⇨ **(photo+signature)**

European Commissioner responsible for Enterprises policy

European SMEs, unquestionably the driving force for employment and growth, are indispensable for the construction of a cohesive Europe and for the development of the Single Market. They generate two thirds of all jobs adapt more rapidly to changes and are a major contribution for regional and local development.

The essential role which SMEs play in Europe is the result of a competitiveness based on a high level of quality of services and products.

The third Multiannual Programme in favour of SMEs aims to support and to reinforce the development and employment potential of SMEs within the European Union as well as internationally, particularly through developing Subcontracting partnerships - i.e. by improving cooperation between purchasers and suppliers.

Against this background, I welcome the joint UNICE and DGXXIII initiative embodied in the Guidelines for Partnership in Industrial Subcontracting. The emergence of a new European approach to industrial Subcontracting in response to economic and trade globalisation holds major development potential. Translating this potential into reality hinges on innovative inter-enterprise relationships, i.e. on close cooperation and stronger partnership between purchasers and suppliers starting at a stage well upstream of production.

The Guidelines for Partnership in Industrial Subcontracting represent an important initiative setting out a consensus-based code of practice and management rules for the parties throughout the whole supply chain. Far from imposing constraints on the partners, these essential "rules of the game" are designed as an aid to choosing and preparing the ground for Subcontracting.

I hope these guidelines will help bring about enduring and more effective inter-enterprise collaboration as a source of fresh impetus in Europe's bid to meet the challenges of newly emerging markets.

GUIDELINES FOR PARTNERSHIP

IN INDUSTRIAL SUBCONTRACTING

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GUIDELINES FOR PARTNERSHIP

IN INDUSTRIAL SUBCONTRACTING[1]

PREAMBLE

In an effort to hold their own in the face of ever intensifying international competition, representatives of purchasers and suppliers within UNICE have formulated these guidelines for partnership in industrial Subcontracting. These guidelines are intended to establish the basic principles and set a recommended framework for partnership between the parties throughout the whole supply chain. The essence of partnering is cooperation between a supplier and a purchaser for their mutual benefit. The most successful partnering arrangements are those built on the competitive strengths of the partners and characterised by factors such as top level commitment, good communications, cultural fit, trust, flexibility and team working.

These guidelines are designed to strengthen the competitiveness of European industry by ensuring co-operative supplier/purchaser relations and fair competition. This would allow the benefits and burdens of change to be shared out on an equitable basis. Even when facing competitive pressures, partners must still respect the generally accepted conventions of good commercial practice. All parties are in agreement that final customer satisfaction should be recognised as the benchmark in all efforts continually to improve products and processes, and that this improvement should be achieved in a spirit of mutual agreement.

Contracts must ensure a fair balance of interests. However, these guidelines do not interfere with contractual freedom between suppliers and purchasers, who may continue to choose the most appropriate legal structures and contractual clauses to organize their commercial relationship. Rather they are meant to serve as a reference for parties negotiating a Subcontracting agreement. They may also serve as a basis for specific sectoral agreements[2] and for legal texts such as model contracts and general conditions.

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1 The term "industrial Subcontracting" refers to all operations where a purchaser buys from a supplier products or services which are specified by the purchaser and form part of the purchaser's products.

2 Such agreements may reflect the particular needs of certain sectors especially of the building industry where the term Subcontracting refers to the execution of part of the works by another contractor on a common construction site in contractual relationship with a main contractor.

1. GENERAL RULES OF COOPERATION

1.1. During the concept and development phase of new products and processes, interested purchasers should cooperate with suppliers in exchanging ideas and information. Both parties must respect the confidentiality of such information.

1.2. The early involvement of suppliers in the development phase should be encouraged.

1.3. Services to be provided during the development phase of a product or process should be defined jointly by the partners, specifying the areas of responsibility and agreeing as to the payment for these services.

1.4. In the event that a purchaser organises a selection phase in which several potential suppliers compete against each other, he should communicate his decision on which supplier has been chosen as rapidly as possible so as to avoid unnecessary expense for himself and for the suppliers not selected.

1.5. In appropriate areas, joint design should take place, and where needed be accompanied by guidance from the purchasers.

1.6. As soon as possible during the development phase, the partners should discuss warranty conditions as well as liability.

1.7. Recognising the potential improvements to competitiveness stemming from the adoption of simultaneous engineering, both partners should strive to increase and improve the application of such processes.

1.8. As appropriate, purchasers should initiate technical assistance programmes to help suppliers adopt new manufacturing methods and improve productivity and quality. Where needed, such technical assistance programmes may include co-operative training.

1.9. Project-related information should be treated as sensitive and confidential. Design information (including CAD data, product/process know-how, process FMEA (Failure Mode and Effect Analysis) should not be disclosed without mutual consent. Exceptions must be provided for in contracts, in detail, and must take into account the interests of both partners.

2. PRICE, COSTS, TERMS OF PAYMENT

2.1. Price, costs

2.1.1. General

Prices should be agreed under conditions of fair competition on the basis of identical requirements notified to competing suppliers. Partners should aim for continuous cost reduction during both the development and the production phases.

It is important to specify which elements and services the price covers, for instance: tools, inspections, buffer stocks, packaging, transport, taxes, warranties, insurance, etc.

The parties should mutually agree on the appropriate price adjustments stemming from changes in specifications or additional requirements (e.g. logistics, warranty) insofar as they influence costs.

The price must also be related to a definite quantity. If the purchaser takes considerably more or less than the agreed quantity, the parties should mutually agree to adapt the unit price adequately.

The same applies if the purchaser deviates considerably from the agreed frequency of call-off[3] and therefore causes unduly large fluctuations (overloads or idle periods) in the supplier's production process.

If the contract is terminated prematurely, the party which had reason to rely on the contract's continuation must be indemnified for its input.

2.1.2. Methods of establishing the price

There are two different methods of establishing the price in a supply contract. If the product is defined from the start, the price may be decided by bargaining. Where the parties co-operate in the development of the product, they may also co-operate in establishing the price by joint cost control.

Bargaining

A price established by bargaining for a given period may not be altered, except under an agreed price adjustment or renegotiation clause. A long-term contract with a fixed price should leave the door open for renegotiation of the price to take into account major unforeseen cost fluctuations.

If the parties intend to prolong a contract which is due to expire they should start bona fide negotiations in good time in order to have the supplies beyond the expiry date covered by an agreement on the price.

[3]By call-off, the purchaser specifies time and quantity of a partial delivery in a long-term contract.

Joint cost control

The fixing by bargaining of market prices for products is increasingly being replaced by joint product and cost planning or control. Wherever the price of the final product is determined by the market from the outset, realistic market opportunities for all those concerned can only be opened up by means of joint product and cost planning or control. Since both parties are interested in the final product being successful in the market, the individual inputs must remain open to value and cost analysis.

Mutual fairness is an essential prerequisite for such cooperation agreements: this is particularly true for the confidential treatment of a partner's special know-how or for allocation of the profits resulting from productivity gains or wider margins.

2.2. Terms of payment

The terms of payment which result from commercial bargaining should be fair to both partners, and should achieve an economic and financial result from which both partners will benefit in the long term.

The best means of ensuring that this occurs is for both partners to put in place good credit management techniques. Responsible companies should:

- have a clear, consistent policy that they pay bills in accordance with contract,
- ensure that both the finance and purchasing departments are aware of this policy and adhere to it,
- agree payment terms at the outset of a deal and stick to them,
- not extend or alter payment terms without prior agreement,
- provide suppliers with clear guidance on payment procedures,
- ensure that there is a system for dealing quickly with complaints and disputes and advise suppliers without delay when invoices, or parts of invoices, are contested.

If the agreed payment period exceeds the time reasonably needed by the purchaser to verify the invoice and arrange due payment, this should be regarded as a credit by the supplier to the purchaser and be taken into account when the price is fixed.

The terms of payment should contain a clause whereby the supplier is automatically entitled to interest at an agreed rate if the purchaser fails to pay the correct amount on time.

3. QUALITY

3.1. Purchaser and suppliers should strive to adopt a common approach to quality within a jointly defined framework. A joint commitment to total quality improvement at all levels should be made by both partners.

3.2. Quality assurance agreements between purchasers and suppliers are looked upon as fair if:

- they make a clear distinction between specifications of a supply and quality assurance methods;
- they contain specifications clearly defined by mutual consent without, however, being ranked as guaranteed product features or warranties; whenever possible the parties should make use of international standards in order to define quality specifications clearly;
- they clearly define the mutually agreed methods by which incoming goods are to be controlled;
- they do not impose unreasonable demands, risks or costs on either party through provisions contained in them regarding; for instance:
    - items subjected to quality controls and procedures for such controls,
    - documentation and record-keeping obligations,
    - alterations to quality requirements or to procedures for dealing with quality problems relevant to the agreed product specifications;
- they satisfy a justified demand to safeguard against any free transfer of know-how through a binding offer to conclude a confidentiality agreement, should the case arise;
- they respect legal rules e.g. about liability for defects or product liability.

3.3. Quality assurance systems gain international recognition if they comply with the standards EN 29000 ff / ISO 9000 ff and if their application is certified at reasonable intervals through audits performed by an accredited certification body (third-party certification). If these conditions are fulfilled, purchasers' audits (second-party assessment) should as a rule only be carried out in the form of process and product audits. Such audits should only assess purchaser-specific processes and products at reasonable intervals or for some justified reason. Duplication of quality assessment work should be avoided through mutual recognition of certification performed by different entities.

4. CONFIDENTIALITY AND INDUSTRIAL PROPERTY RIGHTS

4.1. In a partnership in industrial Subcontracting, each party will acquire confidential know-how from the other. The manufacture and use of products may also involve the use of patents, registered designs**,** computer software and trade marks. The parties are further likely to develop new know-how and acquire new industrial property rights during their cooperation. It is therefore important that the parties agree on their respective right to use and their obligation to protect such confidential know-how and industrial property rights.

4.2. An agreement on know-how and industrial property rights will normally be considered to represent a fair balance of interests if:

- the basic principle applies that the party who works to develop know-how also enjoys the benefits of his work;
- the supplier undertakes to inform the purchaser if, during realisation of the contract, he intends to make improvements or to apply for a patent or other protection for innovations acquired from his own know-how;
- it contains specifications, clearly defined by mutual consent, on patents or other protections for innovations in the supplier's manufacturing technology, resulting from the know-how of both parties;
- each party receives a licence to use the other party's know-how and other industrial property rights to the extent necessary for fulfilling the contract; but that no transfer of proprietary rights to such know-how or industrial property rights shall take place unless the parties have agreed a reasonable payment for such rights;
- the parties are required to treat the other party's know-how as confidential insofar as it has not entered the public domain;
- any restrictions on using the acquired know-how in other contractual relations are in conformity with the applicable rules on competition;
- the party responsible for the design is liable for any infringement of third parties' industrial property rights that may result from the manufacturing, marketing and use of the product. The supplier should, however, not be liable if the infringement is due to the purchaser's instructions or if he has not been informed of the countries where the products will be sold or used.

5. LOGISTICS BETWEEN SUPPLIERS AND PURCHASERS

5.1. The objective of logistics is to optimise the material flow between suppliers and assemblers at all stages, as well as within individual companies - i.e. along the entire value chain of a product - for instance in terms of timing, costs and delivery reliability so as to meet assemblers' needs.

As a rule, optimisation is focused on:

- a rapid material flow (short storage times) with inventories built up and replenished at the lowest possible costs,
- high flexibility to adjust to changes in assemblers' needs.

5.2. Alongside pure supply contracts additional agreements between the parties on communications and other services (logistic services) have recently gained in importance, e.g. agreements on:
- computer-aided exchange of information and the technical preconditions of this exchange,
- allocation and co-ordination of distribution services, possibly by bringing in third parties as suppliers of specialist services,
- pre-treatment or pre-assembly of components or systems,
- installation of systems by the supplier in the assembler's production area.

5.3. Combined supply and logistics contracts require a clear and mutually accepted identification of the goods and services to be supplied, the time and place of delivery, and the moment when risk is transferred. Risks resulting from logistics contracts must

also be taken into consideration. Only a complete statement of the goods and services to be supplied and payment for these goods and services at market prices make it possible to define the best logistics solutions.

5.4. Risk and cost minimisation of supplies and logistic services is above all determined by:

- the maximum and minimum quantity of each delivery, the attendant minimum call-off periods, suppliers' notification periods and delivery intervals,
- the way in which the goods are to be supplied and invoiced (means of transport, place of delivery, packaging, etc.),
- the period within which the purchaser must take delivery of the goods ordered,
- notification periods in the event of changes in, or discontinuation of products,
- agreement on minimum or maximum stocks to be maintained along the logistics chain, especially in the case of forwarders' warehouses and stocks on consignment,
- special requirements regarding quality and the implementation of Electronic Data Interchange (EDI) linked with logistics.

6. SPECIAL MEANS OF PRODUCTION

6.1. Purchase, use and maintenance of the specific means for production (tools, moulds, prototypes, models, profiles, quality control equipment) of the goods to be supplied should be detailed in full and regulated in the contracts. Purchaser and supplier have to consider carefully in their contract appropriate clauses with a view to securing a fair balance of interests. It must be specified whether the purchaser will reimburse the supplier's expenses for production, purchase and maintenance of the special means of production through direct payment or by inclusion in the price of the supplies concerned. The contract should further state the respective obligations of the parties as regards maintenance, repair, insurance and replacement of the specific means of production.

6.2. The partners should from the outset agree on the right to use the means of production so that they fairly reflect the economic effort and input of know-how from both purchaser and supplier with respect to production, purchase and maintenance of the special means of production. The right to use the special means of production placed by the purchasers at the suppliers' disposal should lie with the supplier as long as he uses them for the exclusive purpose of supplying the purchaser.

6.3. The purchaser's legitimate interests may justify his decision to restrict the supplier's right to use the means of production (e.g. by stipulating their exclusive use for the purchaser's order) or to demand that they be handed over. This applies to specific means of production solely owned by the purchaser especially when delivery is unduly delayed or the products supplied are defective, or when the supplier goes bankrupt.

6.4. Particular care has to be taken as well to ensure that manufacturing secrets (know-how) incorporated in the means of production are not used without the prior consent of the entitled party and that reasonable settlement for the manufacturing secrets concerned is guaranteed by mutual agreement.

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