



# **Buyer Guidance for Responsible Contracting**

Transforming engagement with suppliers – from 'risk-shifting' to 'risk-sharing'

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Sofia Menfalout and Anne Lally

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# Responsible contracting

## About this guidance

This resource is part of Fair Wear suite of guidance on responsible purchasing practices, including responsible sourcing dialogue and responsible contracting. It aims at setting the context of responsible contracting in the garment industry, as well as to provide concrete guidance on good practices to follow when reviewing buyer-supplier contracts for HREDD.

## BUYER-SUPPLIER CONTRACTS

### What?

Contracts are legally binding, written documents that set the terms and conditions of doing business between a buyer company and a supplier. The responsible contracting approach focuses on upholding due diligence commitments to preventing and remediating human rights risks and violations through contracts. It is based on a shared responsibility approach which supports more balanced buyer-supplier relations by allocating risks and responsibilities to both parties.

### Why?

A responsible approach to contracting is an important element of due diligence because:

- They are prerequisite tools for **managing risks and implementing HREDD** across supply chains; an enabler for stable, trustworthy and equitable business relationships
- They are the **legal links** of the supply chain
- They make human rights and environmental policies **binding** across supply chain
- They can serve as a **roadmap for legal requirements of responsible purchasing practices**
- They are recommended to **comply with CSDDD**

### Current (irresponsible) practices

Among current contracting practices in the garment industry, we frequently see:

- Business relations that are based on purchasing orders and/or one-way Codes of Conduct
- An absence of contracts/written agreements
- One sided written agreements
- One sided requests from buyer to supplier to implement HREDD through contracts, without buyers supporting their supplier with responsible purchasing practices

- Risk shifting (including financial risks and liability), from buyer to supplier through contracts, e.g. contracts that include unfair payment terms or disciplinary measures
- No accountability, as in traditional contracts contain clauses that support buyers in adverse events such as Force Majeure.

### New standards

Legislative developments in Europe and beyond are requesting buyers to:

- Make responsible contracting a must in their due diligence practices.
- Adopt a shared responsibility approach in line with UN Guiding Principles and OECD Guidelines which includes sharing risks (including financial) and liability with suppliers, e.g. contracts that stipulate buyers' commitments to facilitate HREDD implementation and costing for human rights.

## LEGISLATIVE DEVELOPMENTS

New legislation requires companies to use written contracts with suppliers that not only set the commercial terms of their business, but also integrate and uphold human rights commitments. In Europe, the following legislation require companies to adopt a responsible approach to contracting:

### German Supply Chain Act

The Supply Chain Due Diligence Act (LkSG) includes procurement practices among the preventive measures that companies need to put in place to prevent human rights risks. This includes long-term contractual relationships.

LkSG requirements for contract design:

- Contracts that transfer due diligence obligations to supply chain partners do not meet requirements of effectiveness and appropriateness.
- Instead, companies and suppliers should collaborate on due diligence in light of a shared responsibility approach, to be inscribed in written contracts.
- When designing contracts, companies need to consider the capacity and legitimate interests of suppliers.
- Contractual assurances as preventive measures alone are only rarely effective and appropriate, so they need to be combined with other preventive measures (e.g., responsible purchasing practices).

The German Supply Chain Act also emphasises that it is not possible for companies to fulfil due diligence obligation by simply referring to written assurances from the supplier or by providing generalised declarations of clearance. This means that the use of contracts need to be accompanied by concrete due diligence practices. Buyers can consult the [BAFA handbook](#) for details.

## CSDDD (Approved text 15.04.2024)

Preamble 66 of the approved CSDDD text refers to “a clear allocation of tasks between contracting parties and ongoing cooperation, in a way that avoids the transfer of the obligations provided for in this Directive to a business partner and automatically rendering the contract void in case of a breach”, as well as highlighting the complementarity of use of responsible contracts with other due diligence practices: “the principle that the mere use of contractual assurances cannot, on its own, satisfy the due diligence standards provided for in this Directive”.

**Article 18 and 20 refer to the use of Model Contractual Clauses to support appropriate preventive measures following the key principle of not shifting risks and responsibilities onto suppliers.**

Buyers can consult the [approved CSDDD text](#): Preamble 66, as well as articles 18 and 20.

## European Model Clauses

To support the implementation of LkSG, CSDDD and any mandatory HREDD frameworks, a set of European Model Clauses is being developed, which will serve as reference for the implementation of existing and future European legislation on contracting. Buyers can find more information [here](#). The final version of the EMCs will be ready in December 2024-January 2025.

Fair Wear collaborates with the [Responsible Contracting Project](#) (RCP), a non-profit interdisciplinary team which includes legal experts specialised in responsible contracting for global supply chains. RCP is a member of the European Working Group who is developing the European Model Clauses.

## CONTRACTS AND PRACTICE

Contracts alone do not ensure effective due diligence and need to be supported by action. Contracts can always serve as the basis for a discussion on the issue and for coming to a solution that mitigates or prevents the impact on the supplier and on workers. For example, if a buyer provides long payment terms, a supplier will need to prefinance materials, wages, and overhead well before they receive the buyer’s payment, which results in financial instability. If the supplier is facilitated into providing

feedback to the buyer without fear of retaliation through ongoing responsible sourcing dialogue, they may raise the issue and the two parties may look back at the contractual agreements to find a solution, e.g., decreasing the payment terms length.

For a responsible approach to contracting, the business relation needs to:

- Be founded on shared commitments from both parties, which are exchanged during responsible sourcing dialogue (more information in Fair Wear’s Guidance and Tools for Responsible sourcing dialogue);
- Be supported by responsible purchasing practices.



### Responsible sourcing dialogue

Throughout a business relation, buyer and supplier need to engage in responsible sourcing dialogue to determine if they share the same values, negotiate a contract, define the terms of their collaboration, and more. Responsible sourcing dialogue is a way for both parties to know what to expect from the other side – not only in commercial terms, but also when it comes to long-term roles, responsibilities, and commitments to human rights. A contract translates the outcomes of those due diligence commitments in legally binding written documents. Buyers can use Fair Wear Sourcing dialogue Guidance and Tools to learn how to engage in responsible sourcing dialogue.

### Responsible purchasing practices

To put into practice the commitments to respect human rights stipulated in responsible sourcing dialogue and contracts, buyers need to engage in concrete sourcing actions and responsible purchasing practices (RPPs). RPPs encompass design and product development, planning and forecasting, contracts, technical specifications, order placement and lead times, cost and price negotiations, payment terms, as well as the underlying behaviour, values and principles of purchasers which impact

suppliers and ultimately workers lives. [The Common Framework for Responsible Purchasing Practices](#) is a reference point for companies, which includes several tools for buyers to improve their purchasing practices.

## How to start

Fair Wear expects members to set their commitments to human rights in written agreements with any new business partner. Improving (or introducing) contracts with the goal of HREDD is a lengthy process. It requires alignment between departments (legal, CSR, sourcing/purchasing, etc) within the buyer (and their intermediaries) and involvement of top leadership.

### PRECONDITIONS

Contracts truly prevent human rights risks only when they are supported by action. For this reason, when deciding to improve (or introduce) contracts, buyers should be willing to:

Adopt responsible sourcing strategy that focuses on building quality long term business relations supported by long term contracts. Predictability and consistency of orders in the long term ensures suppliers' financial stability, who in turn are more likely to truly invest in due diligence.

Conduct responsible sourcing dialogue with suppliers. Before placing the first (or additional) purchase order(s) with a new supplier (or a current supplier with whom the buyer has not used contracts before), both parties should agree to the use of two-way written contracts. Buyers can use the Fair Wear Sourcing dialogue Guidance and Tools to learn how to conduct responsible sourcing dialogue.

Engage in responsible purchasing practices. Buyers can use [The Common Framework for Responsible Purchasing Practices](#) as a reference.

Engage with suppliers with a collaborative attitude, treat them as equal partners when negotiating which contract clauses are best suited for your business relation and can benefit both parties.

Involve legal, CSR and sourcing department when reviewing and/or improving their contracts.

Engage with additional departments that correspond with suppliers and may have impact on responsible purchasing practices (i.e. merchandising and design).



## GOOD PRACTICES

Contracts will look different for each buyer, and for each business relation a buyer has with each supplier. The following information is not meant to be prescriptive, but only provide indications on good practices. Buyers should always consult legal experts when drafting or improving their contracts. Fair Wear collaborates with the [Responsible Contracting Project](#) (RCP), a non-profit interdisciplinary team which includes legal experts specialised in responsible contracting for global supply chains, who provides advice to buyers. When improving their contracts, buyers can consult the [RCP Toolkit](#), which includes several sets of model contract clauses and template codes of conduct. For supplier engagement, we recommend the supplier model contract clauses ([SMCCs](#)) which can be adapted to user's needs with a drafting and implementation guidance, as well as the Buyers' Code of Conduct in addition to the Supplier code of conduct. RCP tools are modular, acknowledging that one size does not – and should not – fit all.

### Type of contract

Fair Wear and Responsible Contracting Project recommend using:

A “master agreement” or “framework agreement” under which individual purchase orders are issued. The master or framework agreement is assumed to include all commercial terms, including remedies and human and environmental rights commitments.

CoCs (supplier code and buyer code of conducts, or a two-way code of conduct) as appendices to the master agreement. Buyers can use the [Buyer Code of Conduct template](#) created by RCP as a reference for improving their CoC; and the [SAI Buyer-Supplier mutual code of conduct](#) as a reference for what a two-way CoC may look like.

[Supplier Model Contract Clauses](#) (SMCs) by RCP as a basis for clauses to be negotiated with suppliers. The SMCs were created to improve human rights in apparel and textile supply chains. As a counterbalance to conventional contracting which focuses on suppliers' responsibilities and promises of perfect compliance, the SMCs were developed to address unfair contract terms and purchasing practices that often drive negative human rights outcomes in the supply chain. The SMCs include several buyer responsibilities and purchasing practices connected to human rights outcomes. While the SMCs can be edited to suit the user's needs, RCP suggests all the clauses should be used as written for optimum HREDD. Rather than copying and pasting the SMCs into the contract, users should (1) select the SMCs they want to include in the contract (if not all) and (2) edit and adapt them to suit their

needs and specific circumstances. Buyers can read the [SMCs Framing Memo](#) to learn how to use the SMCs, and the [template of contract clauses](#).

## Negotiating the contract

When negotiating a contract, buyers can use the Fair Wear Tools for responsible sourcing dialogue under “Agenda items for contract negotiation”, for topics to be included in the discussion.

### Do’s

Fair Wear recommend that buyers:

- Give suppliers an opportunity to negotiate the terms of the contract to ensure that both parties have a voice in structuring the arrangement and in advancing their human rights objectives.
- Share with their supplier a copy of buyer’s standard contract, and a copy of the SMCs. Suppliers must have access to the SMCs in order to suggest clauses that may not be part of buyer’s sample contracts, so that the negotiation is fairly played out. Then, buyer and supplier negotiate which contract clauses are best suited for their business relation and can benefit both parties.
- Agree on clauses that set fair payment terms (maximum 60 days upon goods being loaded on the vessel<sup>1</sup>) and forecasting, as well as on planning production collaboratively, before any purchase order is placed.
- Agree on clauses that ringfence labour costs into prices to prevent negotiations from negatively affecting wages. Prices should also include all production costs, including costs associated with upholding responsible business conduct; workers’ wages above legal minimum wage and towards wage increase; costs related to Collective Bargaining Agreement when relevant.
- Minimise fines, penalties, cost price reductions, or airfreight at a supplier’s expense.
- If including clauses on penalties, do so only with use of proof of fault for damages and delays upon delivery.
- Include agreements on the provision of materials in the contract.
- Include agreements on remediation and responsible exit (only using force majeure clauses on mutually agreed upon and legally valid grounds where adverse impacts are considered).
- Only use force majeure clauses on mutually agreed upon and legally valid grounds.
- Include clauses that are favourable to both supplier and buyer (see table below).

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<sup>1</sup> Common Framework for Responsible Purchasing Practices

## Don'ts

Buyers should not:

- Offer contracts on a take-it-or-leave-it basis or treat suppliers' questions and negotiations as an automatic rejection of buyer's offer.
- Rely on purchase orders only. Purchase orders, which are largely contracts of adhesion, i.e. take-it-or-leave-it agreements, tend to maximize the rights and interests of the party offering the contract, which may lead to the supplier accepting the terms without negotiation.
- Include hard clauses on suppliers "even if they are never applied".
- Include clauses for obtaining discounts on delivery delays.
- Include clauses that impact unequally on suppliers (see table below), especially clauses applying penalties for delays or damages without proof of fault.

### Examples of contract terms equal vs unequal for supplier

Terms that are equal/ favourable to suppliers	Terms impacting suppliers unequally
<ul style="list-style-type: none"><li>■ payment for audits by buyer,</li><li>■ pricing that covers living wage,</li><li>■ communication and understanding when production is delayed, with efforts to determine the cause for accountability but also to prevent adverse human rights impact,</li><li>■ commitment to long term quality business,</li><li>■ incentives in case of positive evaluation,</li><li>■ advance payments to cover materials,</li><li>■ payment for unused capacity of expedited shipping if member misses deadlines,</li><li>■ payment if suppliers are required to keep stock</li></ul>	<ul style="list-style-type: none"><li>■ in case of delay airfreight needs to be paid by supplier no matter who contributed to delay,</li><li>■ in case of damages supplier needs to pay without proof of fault,</li><li>■ unfair or unclear penalties,</li><li>■ misuse of force majeure,</li><li>■ payment terms longer than 60 days upon goods being boarded on vessel</li></ul>

## BRAND PERFORMANCE CHECK INDICATORS 2.2 AND 2.13

Indicator 2.2 Member Company Sourcing Strategy is focused on building long-term relationships

Fair Wear expects member buyers to commit to long-term and high-quality contractual relationships, which means:

- Committing to consistent orders for a range of at least 3-5 years
- Providing reasonable assistance to suppliers to support the suppliers' involvement in the buyer's HREDD process. Such assistance is part of buyers' investment in long-term, high-quality relationships.
- Providing positive incentives to suppliers to reward (and support) continued good or superior supplier HREDD.

### What clauses?

To integrate these commitments, member buyers should consider including the following RCP's contract clauses in their contracts, upon negotiation with supplier (buyers can consult the clauses [here](#)):

- *SMC 3.10 (Reasonable Assistance)*
- *SMC 3.11 (Positive Incentives)*

These clauses focus on the quality of relationships with suppliers by expecting the buyer to invest in supporting the supplier's adherence to the Supplier Code of Conduct and encouraging continual improvement for HRE performance. These clauses, among others, aim to improve the quality of the buyer-supplier relationship where applicable.

### Indicator 2.13 Member company's written contracts with suppliers support the implementation of Fair Wear's Code of Labour Practices and human rights due diligence, emphasizing fair payment terms.

Fair Wear expects member buyers to have a Responsible Business Conduct (RBC) policy that is clearly communicated to suppliers and integrated into the supply contracts (e.g., the master framework agreement, the buyer's terms and conditions, and other agreements, and supplier manuals). Responsible business practices should be reflected in these documents.

### What clauses?

For effective HREDD, it is recommended that **members adopt all RCPs SMCs into their contracts** upon negotiation with supplier.

Under this indicator, brands are particularly encouraged to consider the following RCPs contract clauses (buyers can consult the clauses [here](#)):

## Shared responsibility

- *SMC 2 Shared Responsibility to Carry out HREDD* – joint commitment to HREDD in which buyer and supplier each covenants to establish and to cooperate in maintaining a HREDD process.

## Buyer obligations

- *SMC 3.6 Pricing* – buyer and supplier shall collaborate to agree on a price, taking into account the scope and size of the contract, that accommodates the costs associated with upholding responsible business conduct, including the payment of a Living Wage to workers.
- *SMC 3.9 Order Changes* – for any change to an agreed order (including, but not limited to, cancellations, change orders, quantity increases or decreases, or changes to design specifications) requested by Buyer or Suppliers, Buyer and Supplier shall consider the Adverse Impacts.
- *SMC 3.7 Commercial Terms: Payment & Delivery* (references BPC Indicators 2.13, 2.16, 2.17, 3.10, 3.11, 3.13) – buyer shall collaborate with suppliers to agree on commercial terms, including payment and delivery terms, that will support Buyer’s and Supplier’s performance of their respective obligations under this Agreement and prevent and mitigate Adverse Impacts.
- *SMC 3.12 Charges, Penalties, and the Like* – the parties shall specify at the outset any charges, price reductions, chargebacks, penalties or the like (the “Charges”) that will be levied by Buyer in the event of delays, non-conformity of the goods, or any other default (including a HREDD-Related Default) or breach of this Agreement.

## Adverse impacts, remediation & responsible exit

- *SMC 5 Adverse Impacts and Corrective Action Plan* (references BPC Indicator 3.1, 3.6, 3.7 and 4.5) – where an actual Adverse Impact has occurred, the parties each agree to perform the following HREDD Obligations within a Corrective Action Plan.
- *SMC 9 Responsible Exit* (references BPC Indicator 3.17) – in any termination of this Agreement by either party, the terminating party shall consider the Adverse Impacts, collaborate with the other party to address such Adverse Impacts and employ reasonable efforts to avoid or mitigate them, and provide reasonable notice to the other party of its intent to terminate this Agreement.