

Quality Assurance Agreements under ISO/TS 16949 – liability risks and avoidance strategies

By Dr. Ekkehard Helmig, Wiesbaden, Attorney-at-Law, and Sven Regula, Wiesbaden, Attorney-at-Law. The original has been published in Phi, Produkthaftung International 5/2012

Contracts in the automotive industry have been gripped by a recourse claim mania. They are mainly based on hubristic demeanor, i.e. those contracting partners who enjoy a position of power and thus can impose the strictest conditions on their suppliers are deemed guarantors of product quality, pretending defects could not occur within their realms; it is assumed only subordinate suppliers produced defects which the powerful contracting parties did not or could not have noticed in time, the result of this being the suppliers' obligation to pay. The increasing number of recalls in the automotive industry refutes the assumption that rigorous contracts and cost pressure directed downstream enhanced the vehicles' quality¹. Quite the opposite is true: Root causes which have led to defects and thus recalls are often due to a complex set of reasons always including the vehicle manufacturer as the last link of a chain of responsibilities with respect to a vehicle's quality. Usually, root causes cannot be traced to one single activity or error in the supply chain.

Each error made at some level in the supply chain that remains undetected causes a domino effect, the consequences of which become all the more severe the earlier the error has been produced and the later it has been detected. Defective and often unlabeled mass production parts such as screws, springs, electric switches, sensors or sintered parts in seat belts or ABS systems are prone to remain unnoticed until such time as an accident has occurred leading in turn to a recall. There is no absolute guaranty of errors not to occur in electric and electronic components or systems, anyway.² Quality Assurance Agreements (in the following referred to as QAA) are to counteract these developments by establishing rules for avoiding defects; these rules are primarily set up at bilateral contract level, their effects however, apply to the entire supply chain.

1. Functions of QAA

The primary goal of QAA between customers and suppliers – this generally applies to all technical industries – is to avoid defects as defined by Section 3 of the German Product

¹ Helmig, "Rückruf für die Vertragswerke in der Automobilindustrie" (Recall of contracts in the automotive industry), ZfAE 2007, p. 36.

² ISO 26262 Functional safety; for more details see: Helmig, "Fahrzeugsicherheit versus Fahrerunsicherheit – Kritische Überlegungen zur KVV und zur ISO 26262" (Vehicle safety vs. driver uncertainty. Critical thoughts on design responsibility agreements and ISO 26262). In: PHI 2010, p. 194; Furthermore: "Functional Safety in accordance with ISO 26262 and product liability for No Trouble Found events", <http://www.notar-helmig.de/de/publikationen.html>.

Liability Act (ProdHaftG) as well as material defects as defined by Sections 434 and 633 of the German Civil Code (BGB). Where defects and/or material defects occur in the supply chain, they need to be detected as early as possible so as to prevent more damage in the upstream supply chain. Therein consists the principal preventive function³ of QAA.

QAA have another function which is of great importance in practice, yet widely disregarded among legal literature, that is their function to shift the buyer's statutory burden of proof, regarding the time at which the defect or material defect occurred, to the supplier⁴ (reversal of the burden of proof function). QAA often set out that the statutory liability for defects and/or material defects be imposed solely on subordinate suppliers (so called apportionment of liability function⁵). Furthermore, QAA serve business purposes such as saving costs by rationalization (so called rationalizing function⁶) as well as purposes of safeguarding guaranties which vehicle manufacturers extend to final customers in order to make a product competitive from the point of view of costs (guaranty recourse safeguarding function)⁷. The latter is not discussed in the relevant legal literature, either⁸. Finally, QAA often oblige suppliers to be able to trace products delivered by them within their own production (traceability function).⁹

2. The legal character of QAA

The categorization of QAA (and thus the basis of liability established by QAA) is controversial from the viewpoint of legal dogma¹⁰. They are special contracts which cannot be related to

³ Kreifels/Weide, *Produkthaftungshandbuch (Product liability compendium)*, Section 57, note 4, 3rd edition, Munich 2012.

⁴ For instance, Kreifels/Weide's, *ibid.*, very detailed explanation of QAA does not cover this aspect.

⁵ Kreifels/Weide, *ibid.*, Section 57, note 5.

⁶ Kreifels/Weide, *ibid.*, Section 57, note 3.

⁷ The product's final price is not burdened by guaranty costs incurred by recourse claims against the supplier. As a consequence, the automotive industry in particular is governed by ever longer periods of notice regarding warranties that are beneficial to final customers as well as by rigid recourse regulations across the supply chain which far exceed legal provisions according to Sections 478 ff of the German Civil Code (BGB).

⁸ See for instance Kreifels/Weide, *ibid.*

⁹ Ensthaler/Gesmann-Nuissl/Müller, *Technik-Recht (Technology Law)*, Springer, 2012, p. 139 f, also address four principal functions of QAA: the preventive function, the rationalizing function, the perpetuating function and the apportionment of liability function. With respect to a QAA's legal qualification see p. 186 ff. Ensthaler/Gesmann-Nuissl/Müller (p. 189) consider QAA to be contracts which impose more obligations on one party in order to protect the other party's interests without this being fixed by concrete contractual obligations to perform. As contractual obligation in return a special duty of loyalty is established for both parties. The reasons, aiming only at one party's interests from the viewpoint of legal dogma, neglect the process-oriented approach of what QAA are supposed to regulate: the manufacturing of products in a harmonized fashion so as to manufacture final products free from defects. This approach goes beyond a merely bilateral point of view.

¹⁰ For details on current opinion see: Kreifels/Weide, *ibid.*, Section 58, note 8 ff.

any type of contract set out in the German Civil Code (BGB)¹¹. The contracts regulated by the German Civil Code, e.g. contracts to produce a work, service contracts and purchase agreements, establish claims on performance in compliance with the contract. However, the German Civil Code does not set out claims which give the obligee the right to demand requirements regarding the suppliers' organizational infrastructure as precondition for their worthiness to supply goods, i.e. requirements which need to be fulfilled before the actual performance of the contract takes place and the perpetuation of which can be proven to the customer by dint of his contractual right to auditing at any time.¹² Whereas all contract-specific legal regulations regarding defaults in performance and breach of contract always require performance of the contract, which these organizational conditions do not include, QAA privileges the obligee to demand an organizational and process-oriented safeguard to ensure the performance be in compliance with the contract even before the performance itself has been initiated. The compliance with infrastructure and work environment as agreed upon by contract or changes thereto are contractual obligations before the performance of the contract takes place by delivering products. Therefore, where violations of these contractual obligations deriving from QAA occur, German liability law governing material defects in breach of contract for purchase agreements or contracts to produce a work is not applicable but the general regulations regarding defaults in performance and breach of contract as set out by the German Civil Code¹³.

3. ISO/TS 16949 as integral part of QAA

- a) Establishing QMS in compliance with ISO/TS 16949 and the contractual obligation to produce accordingly

In the automotive industry suppliers need to have effective quality management systems (QMS) in compliance with ISO/TS 16949. This Technical Specification, which is to be applied as a general rule in the automotive industry, is based on the international standard DIN EN ISO 9001:2008, including additional requirements specific to the automotive supplier industry; as such it sets out rules in order to be the "traffic road regulation" applicable to all activities and levels in the supply chain. ISO 9001:2008 states: "This International Standard specifies requirements for a quality management system where an organization (a) needs to demonstrate its ability to consistently provide product that meets customer and applicable

¹¹ See Lehmann, Just in time: Handels- und AGB-rechtliche Probleme, Verlagerung der Wareneingangskontrolle und Öffnung der Qualitätssicherungsvereinbarung (Just in time: problems regarding trade law and terms and conditions law, shifting incoming goods inspection and opening quality assurance agreements), BB 1990, p. 1849 ff. For a different opinion see: Kreifels/Weide, *ibid.*, Section 58, note 14.

¹² For instance, ZF's directive on quality management QR83 states in its introduction: "This section describes the requirements for the management system of the supplier" and "an effective quality management system set up according to the standards and regulations of ISO/TS 16949 is a prerequisite for supplier relations with ZF". <http://www.zf.com>

¹³ Different opinion: Kreifels/Weide, *ibid.*, Section 58, note 14.

statutory and regulatory requirements, and (b) aims to enhance customer satisfaction through the effective application of the system ...".¹⁴ As for the automotive industry, ISO/TS 16949 "in conjunction with ISO 9001:2008, defines the quality management system requirements for the design and development, production and, when relevant, installation and service of automotive-related products".

In the past, it usually sufficed where suppliers undertook to set up QMS in compliance with QS 9000 or subsequently ISO/TS 16949 and have their QMS certified by a certification body. Any shortcomings of the QMS were audited by the certification body in the course of surveillance audits or recertification audits. However, direct and legal entitlements deriving from contracts and impending sanctions therein to demand compliance with ISO/TS 16949 requirements were not issued.¹⁵

Meanwhile, QAA in which customers and suppliers expressly establish ISO/TS 16949 in its entirety as integral and mutually binding part of their contract are becoming ever more frequent. In addition to the QMS requirements according to ISO/TS 16949, most vehicle manufacturers set up further requirements with respect to QMS ("Customer Specific Requirements" – CSR¹⁶). From the point of view of liability law a completely new situation arises for both parties: Noncompliance with ISO/TS 16949 requirements becomes a breach of contract for both parties and thus constitutes the right to claim damages according to Section 280 of the German Civil Code (BGB) irrespective of the liability for product quality.¹⁷ Violations of contractual obligations can take place at two levels in particular:

- (i) the organizational structure as required by ISO/TS 16949 in order to establish an effective QMS, including management responsibility and the provision of human and material resources and
- (ii) the product realization and manufacturing processes, including all additional requirements such as measurement quality and continual improvement.¹⁸

¹⁴ ISO 9001:2008 – 1.1

¹⁵ In practice, formal certification and proving the ownership of a valid certificate have been attached great importance to. Yet, legal consequences have rarely ensued.

¹⁶ According to the VDA Standard "Establishing customer-specific QM system requirements based on ISO/TS 16949", 1st edition, 2010, ed.: Verband der Automobilindustrie e.V. (VDA), Customer Specific Requirements are additional and/or expanded QM requirements relevant to the system and complementing generally valid certification requirements according to ISO/TS 16949 or equivalent certification criteria (e.g. VDA 6.1) in their respective latest versions.

¹⁷ In Point 9 of its international terms and conditions for the purchase of production materials and automotive components, BMW expressly determines ISO/TS 16949 to be valid and applicable. Almost all contracts drafted by vehicle manufacturers require QMS in compliance with ISO/TS 16949 as a precondition. Large suppliers, such as ZF with its QR83, determine their own suppliers' capability of achieving quality by precisely referring their requirements to ISO/TS 16949 provisions.

¹⁸ These two levels have already been determined by ISO 9001 which is applicable to all quality management systems and forms the basis for ISO/TS 16949. In practice though, it is a common myth that ISO/TS 16949 comprised solely unilateral obligations of the supplier towards the customer. The ISO/TS 16949 concept of all processes being in "interaction" alone, which applies to the entire value chain, is one diametrically opposed to this unilateral concept and violates the higher principle of avoidance of errors. For more details see: VDA-Band 5 "Prozesseignung" Eignung von Messsystemen etc. ("Process capability" capability of measurement systems etc.), 2nd edition, 2010, ISSN 0953-9412.

Therefore, QAA based on ISO/TS 16949 do not only stipulate essential organizational structures of a company as a prerequisite, but determine them as binding condition agreed upon by contract and applicable to the performances of design and development, manufacturing, delivery and further processing of products as defined by ISO 9001:2008 - 1.1. This contractual character of the organization is not limited to bilateral customer-supplier-relations only, but also oriented towards an avoidance of defect strategy in the entire supply chain. ISO/TS 16949 is a process-oriented standard applicable to the entire supply chain. Agreements on the quality management system's organization in accordance with ISO/TS 16949 requirements apply to all links in the supply chain, including vehicle manufacturers¹⁹; by doing so, the conformity of the organization is to ensure conformity of the product realization processes, which in turn serves as a precondition for a generally applicable and reliable production and manufacturing process management based on division of labor.²⁰

b) The minimum of what QAA need to regulate

First and foremost, QAA need to ensure communication between customer and supplier as basic requirement of the standard. In most QAA known to the writers this fundamental issue is not addressed at all.

Since ISO/TS 16949 has been agreed upon as integral part of the QAA, ISO/TS 16949 determines those obligations on the company's part, the latter being one of the contracting parties, which are to be fulfilled by the QMS at production realization level according to Chapter 7 of ISO/TS 16949. The QAA thus links all agreements concluded in customer-supplier-relations, which includes the entire company as well as its management.

Where ISO/TS 16949 forms an integral part of QAA²¹, the standard's basic principle of avoidance of defects needs to be implemented by both sides, in particular by means of the obligatory internal communication, i.e. at company level, as well as customer communication as set out by ISO/TS 16949. At internal company level, communication is to ensure the QMS's effectiveness as prerequisite for customer communication. Point 5.5.3 determines: "Top management shall ensure that appropriate communication processes are established within the organization and that communication takes place regarding the effectiveness of the quality management system." By using the phrasings "ensure" and "takes place" ISO/TS 16949 implies continual confirmation of effectiveness and efficiency of all measures taken, which is to serve as precondition for the QMS's capability to manufacture products according to the quality that has been agreed upon.

In Chapter 7.2.3 (Customer communication) ISO/TS 16949 addresses external customer-relations and sets out that arrangements shall be determined and implemented in order to communicate with customers in relation to product information, enquiries, contracts or order handling, including amendments and feedback. The supplier's obligation to initiate

¹⁹ See footnote 17 and the example of BMW.

²⁰ ISO/TS 16949 - 0.2 Process approach.

²¹ Even where the application of ISO/TS 16949 is not expressly agreed upon by contract its general application is nonetheless effective. The standard is well-established to the extent that it can be deemed generic and generally applicable.

communication with customers is necessarily just as substantial as the customer's obligation to contribute to these communication processes, the latter primarily serving the purpose of defining the component to be delivered as well as its manufacturing process.

Communication serves the purpose of ensuring that the nature and quality of the product to be delivered shall be as agreed upon by contract (Section 434 (1) sentence 1 of the German Civil Code [BGB]) or ensuring the product shall be suitable for the purpose and intended use under the contract (Section 434 (1) sentence 2 No. 1 of the German Civil Code). The regulations of ISO/TS 16949 on communication are not intended to define a material defect in breach of contract as defined by Section 434 of the German Civil Code. They are conducive to avoid such material defects as defined by Section 434 of the German Civil Code primarily by means of communication. Where suppliers are obliged to determine "requirements related to the product" due to Point 7.2.1 of ISO/TS 16949, they as experts must raise all relevant issues which are relevant to the product's nature and quality under the contract. In the event of gaps in the customer's specifications, suppliers need to determine and complement all requirements necessary for the purpose and intended use specified in the contract. Customers' responses must be adequate as well as correspond to the suppliers' solutions to meet so as to the statutory requirements as to be deemed a specification in a legal sense.

Where QAA include ISO/TS 16949 the product- and manufacturing process-specific bases for "communicating with customers"²² are laid with respect to the legal relations between the two parties; by doing so, the two responsibilities of the parties which are essential to communication are established: The supplier's²³ responsibility to ask as well as the necessary and just as crucial responsibility to response by the customer; these two aspects form a synallagmatic relationship consisting of an obligation to collect (responsibility to ask) and an obligation to deliver (responsibility to response). The nature and quality (specification) of a product to be delivered can only be considered as legally agreed upon according to Section 434 (1) of the German Civil Code where it has been determined as a result of corresponding questions and responses.

Insufficient questions on the supplier's part constitute a breach of contract according to Section 280 of the German Civil Code. Where the customer refuses to communicate he is not entitled to claim the supplier's performance and violates his own contractual obligations according to Section 280 (1) of the German Civil Code²⁴; as a consequence of this refusal to communicate the supplier may assert claims against the customer, for instance where expenses incurred in vain.²⁵ These legal consequences due to breach of contract are

²² ISO/TS 16949 - 7.2.3

²³ ISO/TS 16949-7.2.1 "Determination of requirements related to the product".

²⁴ The communication process as required by ISO/TS 16949 manifests itself in a number of other rules and standards of comparable status: VDA's publication "Das gemeinsame Qualitätsmanagement in der Lieferkette – Produktentstehung – Reifegradabsicherung für Neuteile" (Joint Quality Management in the Supply Chain – Product Creation – Maturity Level Assurance for New Parts), 2nd edition, October 2009, ISSN 0943-9412, is intended to ensure and validate the quality of the entire scope of supply as agreed upon by contract by means of a systematic procedure which entails checking well-defined measurement criteria at each maturity level, the latter being organized according to the vehicle manufacturers' overall project plan.

²⁵ In practice, insufficient communication occurs rather frequently. It is not unusual that suppliers wait in vain for a customer to confirm amendments that have been agreed upon; the same holds true for approvals of First Article Inspection Reports (FAIR). The supplier's only resort is to deliver

irrespective of those legal consequences resulting from manufacturing and delivery of defective products.

QAA need to state communication obligations so that the responsibilities to ask and response can be met in terms of processes documented thereto as well as persons in charge so as to define the interface between verification and validation: Verification answers the relevant questions at component level and thus supplier level, i.e. whether the supplier has fulfilled his obligation, the latter agreed upon in bilateral communication, and whether his component is functioning. Validation is always the customer's responsibility and decides at his level of the system whether the component satisfies the system's requirements and hence corresponds to the required functionality.²⁶ The processes of verification and validation include risk analyses as well as the coordination of Failure Mode and Effects Analysis (FMEA).

The decisive legal consequence thereof is that claims on grounds of violation of the obligation to communicate according to QAA follow the regular limitation period as defined by Section 194 of the German Civil Code and the regular limitation period only commences as of the person's knowledge of the circumstances which have brought about the claims.

c) The decisiveness of the parts history documentation

QAA have to encompass requirements for these responsibilities to be reconciled and for the results to be congruous as well as documented by means of a parts history documentation. Therefore, the parts history documentation is among the most crucial documents; it constitutes the common understanding in the development and in the change management of a product and leading straight to the effectiveness of the stringent processes set out in ISO/TS 16949 on which the QAA has been based and which have been required and agreed upon.

The parts history documentation, as part of the bilateral contract, has two essential functions: (i) With respect to the fulfillment of the contract it documents each binding version of agreements on the quality and nature of the product (specification) as well as all amendments, modifications or changes that were agreed upon. It documents the agreed change management and determines each change or revision index effective for engineering drawings and technical documents. (ii) Furthermore, the parts history documentation is the most essential tool to safeguard evidence effective for the entire supply relationship. As for product realization, the compliance with all required inspections, tests and measurements, including methods and procedures carried out thereto, derive from the parts history documentation.²⁷ In practice however, detailed provisions on parts history documentations are scarcely to be found.

up-to-date parts history documentation as well as to point out his waiting for response together with the delivery or to emphasize the submitted but not yet approved FAIR. Where the customer accepts the delivery without objection an implied approval can usually be assumed.

²⁶ ISO 9000:2005 - 3.8.4 and 3.8.5 define the terms "Verification" and "Validation".

²⁷ The parts history documentation is a deed under German law with its probative force assigned by Section 416 of the German Civil Procedure Code (ZPO). In the automotive industry it is integrated into numerous contracts to fulfill precisely this function. In the design responsibility agreements of Volkswagen AG, a prerequisite in order to conclude a supply contract, the parts history

d) Waiving the incoming goods inspection

From a historical point of view, one of the reasons to conclude QAA was Purchasing's primarily cost driven intention to not carry out incoming goods inspections as defined by Section 377 of the German Commercial Code (HGB) at all or to postpone them immensely. The 8th civil panel of the German Federal Court of Justice (BGH) decided in its ruling on June 19, 1991²⁸, that a waiver of an estoppel under German law due to an incoming goods inspection not carried out was impermissible in general terms and conditions if it led to immediate notice of apparent defects not being necessary anymore.²⁹ Thereupon, literature suggested incoming goods inspections could only be waived where an agreement with the supplier had been made assuring the Buyer would not be delivered defective goods.³⁰ Hence, in most QAA regulations can be found which make the supplier waive his right to an estoppel due to notice of defects issued too late according to Section 377 of the German Commercial Code.

This waiver of Section 377 of the German Commercial Code cannot be reconciled (any longer) with the now applicable priority and effectiveness of ISO/TS 16949 in contracts.³¹ Where ISO/TS 16949 is applied to a contract, Point 7.4.1 of the standard (purchasing process) sets out an obligatorily required process whereby the customer must **ensure** prior suppliers have delivered defect-free goods by taking appropriate measures targeted at this end. The customer can fulfill this requirement either in a product- or manufacturing process-specific fashion at the time of receipt of the goods or during production processes. In the event of a customer having bought goods which later on turn out to carry defects that were caused by prior suppliers, prima facie evidence is established, i.e. it is assumed the customer has not taken appropriate measures to ensure he is delivered defect-free parts. According to Section 280 of the German Civil Code (BGB) he is liable towards his own customer at the next level of the supply chain. This liability is in force irrespective of warranty or product liability for material defects of the product or manufacturer's liability.

Due to the system of interaction between all processes set out by ISO/TS 16949 (Point 0.2) neither Point 7.4.1 nor Point 7.4.3 can be waived without influencing and rendering

documentation is subject to strict written form requirements so as to document its great importance for the latest content of the binding agreement. For more details on design responsibility agreements: Helmig, "Die Konzeptverantwortungsvereinbarung von VW im Konflikt mit Angemessenheit und Transparenz" (VW's design responsibility agreements in conflict with appropriateness and transparency), PHi, 2009, p. 30.

²⁸ Federal Court of Justice (BGH): NJW 1991, 2633 f; the 10th panel of the BGH sustained this legal practice in its ruling on September 17, 2002, X ZR 248/00, BGH Report 2003, p. 285 ff., stating that where an objectively required and reasonable kind of inspection does not correspond to what is customary in a given industry, such action shall not deserve protection.

²⁹ The 10th civil panel of the BGH declared a general waiver of an incoming goods inspection impermissible in its ruling on September 17, 2002, X ZR 248/00.

³⁰ See for instance Balsmeier, Deutschland: „Qualitätssicherungsvereinbarungen in der Praxis“ (Quality assurance agreements in practice), in: PHi 99, p. 160, p. 164 f.; Kessel/Passauer: „Einkaufsbedingungen in der Automobilindustrie“ (Terms and conditions of purchase in the automotive industry), in: Betriebs-Berater, 2004, 19974, 1975; Kannoowski, in: Betriebs-Berater, 2007, 2301.

³¹ For more details see: Helmig, „Die ISO/TS 16949 steuert den Sachmangelregress in der automotiven Zulieferkette“ (ISO/TS 16949 governs recourse claims on grounds of material defect in the automotive supply chain), PHi, 2011, p. 81, 89.

ineffective the standard's stringent processes and their higher goal of avoidance of errors.³² The obligations relating to inspection set forth in ISO/TS 16949 - 7.4.1 and 7.4.3 are absolute and unconditional as more specific provisions by dint of their reference to the manufacturing process. Section 377 of the German Commercial Code or a waiver thereof do not alter the binding character and priority of the ISO/TS 16949 requirements in the least.

The delivery of defective components usually gives rise to the customer's assumption that the supplier has violated Point 7.4.1 of ISO/TS 16949, hence entitling the customer to claim damages of unlimited amount against the supplier according to Section 280 (1) of the German Civil Code.³³ The obligation to ensure that parts to be purchased are defect-free according to ISO/TS 16949 - 7.4.1 corresponds to the obligation of verification of purchased products according to ISO/TS 16949 - 7.4.3. The standard therein states that all measures and inspections "necessary for ensuring that purchased product meets specified purchase requirements" shall be carried out. The extent of the inspection corresponds to the product specific inspection obligations as defined by Section 377 of the German Commercial Code, the latter being the stricter the more safety relevant a product is or the greater subsequent damages could be if inspections were not carried out.³⁴

In a recourse trial where customer A asserts claims against his sub-supplier B it seems likely for sub-supplier B to claim customer A's severe contributory negligence as defined by Section 254 of the German Civil Code to have contributed to the occurrence of subsequent damage due to an omitted incoming goods inspection with reference to Points 7.4.1 and 7.4.3 of ISO/TS 16949.³⁵ However, where sub-supplier B objects and rebuts according to Section 254 of the German Civil Code (BGB) although he has completely released customer A from or postponed his duty to carry out incoming goods inspections according to Section 377 of the German Commercial Code (HGB) as part of a QAA, he acts inconsistently due to the QAA's preventive function for the entire supply chain³⁶ mentioned above. By releasing customer A from his duty by means of a contract, sub-supplier B sets a standard of confidence in terms of customer A relying on the fact that the outgoing goods inspection has sufficiently ensured the goods were defect-free so as for him to be able to not carry out

³² Similar to the VOB/B (German construction contract procedures – Part B: General conditions of contract relating to the execution of construction work) ISO/TS 16949 is to be legally examined from the point of view of laws governing general terms and conditions, even where it is only partly changed. For more details see: Helmig, PHi 2011, p. 84, see footnote 14; Agreeing likewise: Kreifels/Weide, *ibid.*, Section 61, note 4.

³³ Higher Regional Court (OLG) Nuremberg, ruling on November 25, 2009, 12 U 715/09, BecksRS 2010, 00067.

³⁴ A ruling of the German Federal Court of Justice (BGH) states that the Buyer shall first inspect weaknesses of the goods that have been brought to his attention due to prior deliveries before examining the goods for defects they never had before. BGH, ruling on October 14, 1970 - VIII ZR 156/68, BB 1970, 1416; ruling on December 3, 1975, *ibid.*; ruling on April 4, 1977 - VIII ZR 141/75, BB 1977, 1408; ruling on June 6, 1991 - VIII ZR 149/90, NJW 1991, 2623; comment written by several authors (Gemeinschaftskommentar).

³⁵ Under German law incoming goods inspections constitute a duty in the customer's interest for which he cannot be sued, yet by omitting it he forfeits certain rights and can no longer claim them in later disputes. Where the customer violates this duty which serves his own interests, he can hardly assert claims against his supplier as a consequence of his own inaction. Ruling of the German Federal Court of Justice (BGH): BGH X ZR 248/00.

³⁶ See Point 1.1 of ISO/TS 16949.

an incoming goods inspection.³⁷ Not satisfying this standard of confidence is always to the detriment of sub-supplier B. Yet, a differentiation is to be made at this point: Where the contracting parties are on par and meet on a level playing field it can be assumed that liability will be shared proportionately. Sub-supplier B's objection according to Section 254 of the German Civil Code combined with the arguments delivered by ISO/TS 16949 - 7.4.1 and 7.4.3 will be successful in the event of legal relations where customer A, by virtue of his economic superiority, self-servingly insisted on being released from his duty to carry out incoming goods inspections in order to save costs.

If the links of a supply chain accept ISO/TS 16949 as higher-ranking organization requirements and thus implement it in their daily business practices the preventive function of ISO/TS 16949 shall always have priority over a bilateral waiver of incoming goods inspections.

4. Audit tools and audit methods

By making ISO/TS 16949 an integral part of a QAA the supplier is provided with a general process structure he needs to adhere to regarding design and development as well as manufacturing of products and manufacturing processes corresponding thereto. However, regulations addressing audit and measurement procedures and methods can barely be found in QAA. If to be found at all, they merely consist of references to customer specific standards. But experience has shown that it is precisely this aspect of QAA which urgently needs to be regulated to stipulate audit and measurement procedures and methods resulting in clear criteria for product- and manufacturing-processes determined thereafter. Using different measurement procedures, for instance, could incur considerable costs for both parties, which can be avoided by comprehensive provisions in QAA. Implementing measurement procedures which have not been regulated and coordinated would in turn constitute a breach of contract entitling the injured party to claim damages according to Section 280 (1) of the German Civil Code (BGB).³⁸

The QAA used in practice are largely recourse claim oriented and do not derive from the process approach of ISO/TS 16949. Yet, QAA can only fulfill their functions to serve avoidance of defects in the supply chain where they follow the guiding principles of ISO/TS 16949 as does, for instance, the above mentioned QR83 by ZF which refers each of the guideline's requirements precisely to the corresponding sections of ISO/TS 16949.

5. Claims deriving from QAA due to delict

a) Final customer's claims

³⁷ Similar: Ensthaler/Gessmann-Nuissl/Müller, *ibid.*, p. 187.

³⁸ In practice this source of errors occurs rather frequently, for instance regarding tolerance: there are often no provisions on how to determine tolerance although this determining largely depends on the audit tools and audit procedures applied which can lead to different results due to common inexactness of measurements. Without precise provisions in a QAA errors are destined to occur. ISO/TS 16949 therefore requires in Point 8.2.3.1 the monitoring and measurement of manufacturing processes, which necessarily includes coordination of audit tools and audit methods.

Under the conditions of a supply chain oriented towards avoidance of defects the waiving of incoming goods inspections or neglecting of processes constitute violations of the duty to take care with respect to final customers (consumers) who trust that the obligation to avoid defects is being complied with. He expects a safe vehicle and does not anticipate that safety related inspections are not carried out due to cost driven motivations in the supply chain. This risk in the supply chain is not indicated to him by either the vehicle manufacturer or other suppliers or the dealer and thus he cannot estimate its implications and therefore cannot cope with it (Section 6 (1) No. 1 of the German Product Safety Act [ProdSG]). The recourse claim scenarios in the supply chain are of no importance to him.

It is (for now) too farfetched to assume QAA establish third party beneficiary contracts or contracts with protective consequences for final customers. But it cannot be denied that QAA based on ISO/TS 16949 are at any rate moving in this direction. Assuming the prohibition to place unsafe products on the market³⁹ and accounting for the BGH's approach in its Airbag decision⁴⁰ the compliance with and implementation of the processes required by ISO/TS belong to the state of the art. It seems logical to take this thought one step further so as to meet the BGH's requirement that structures and devices – they are covered by the processes of product realization – have to be at the state of the art of science and technology. In any case this leads to clear results for all safety-related components, the results being inherent to a QAA.

Noncompliance with a QAA (for now) does not give rise to claims due to delict on the part of final customers. In product liability trials, however, QAA can provide evidence for the causality establishing liability due to the processes deriving from ISO/TS 16949; this can complicate a defense claiming a defect occurred as exception in spite of appropriate and reasonable precautions.

b) Claims according to Section 826 of the German Civil Code (BGB)

The conclusion of a QAA is a contractual agreement which is met under the condition that the contracting parties can comply therewith. This does not go without saying, at least not in the automotive industry. Many medium-sized companies with highly specialized know how are active in this industry. But, as experience has shown, they can often not live up to the industry's requirements set out in contracts and they are often not capable of satisfying QAA's requirement to provide sufficient resources due to financial constraints. In individual cases a risk resulting from such circumstances can lead to liability according to Section 826 of the German Civil Code (BGB) where establishing and passing on severe potential damage is possible and accepted. So far there have been no court decisions relevant to this issue. Yet, the German Federal Court of Justice (BGH) has indicated in its ruling on March 31, 1998, (VI ZR 109/07 transistor – power door locks⁴¹) that accepting the manufacturing and delivery

³⁹ Article 1 No. 1 of the EU Directive on General Product Safety of December 3, 2001, Official Journal of the European Union of January 15, 2002, L 11/4.

⁴⁰ BGH ruling on June 16, 2009 – VI ZR 107/08, NJW 2009, 2953; Helmig: "Die Airbag-Entscheidung im Kontext zum Gemeinschaftsrecht – Vertragsrelevanz für die Automobilindustrie" (The airbag decision in the context of European Union law – relevance regarding contracts in the automotive industry), PHi, 2009, p. 190.

⁴¹ BGHZ 138, 230 = NJW 1998, 1942.

of defective products on a large scale could be judged as intentional damage contrary to public policy as defined by Section 826 of the German Civil Code.

6. Corporate negligence

ISO/TS 16949 stipulates a strict corporate organization in order to fulfill all of the standard's process requirements. The requirements in Chapter 5 (Management responsibility) cannot be discussed in detail in this article for lack of space. Suffice it to indicate that management responsibility for the QMS's functioning under the avoidance of defects condition is essential for the risk management of the entire company (Section 91 (2) of the German Stock Corporation Act). Noncompliance with the provisions of a QAA based on ISO/TS 16949 indicates corporate negligence on the management's part.

7. Insurance

QAA including ISO/TS 16949 as integral part of the contract constitutes a written agreement. The deliberate decision to not provide required resources (ISO/TS 16949 - 6.1 [Provision of resources] and 6.2 [Human resources]) in spite of contractual agreement to implement ISO/TS 16949 can be construed as deliberate noncompliance with written agreements according to Point 6.2.4 of the requirements for product liability insurance, which can compromise the coverage of product liability insurance. Insurance coverage would be particularly jeopardized where a court construed the extended deliberate noncompliance with written and agreed upon quality assurance requirements as intentional unethical damage according to Section 826 of the German Civil Code (BGB).

8. Conclusions

Including ISO/TS 16949 as binding and integral part into a QAA primarily serves the purposes of prevention, reversal of the burden of proof, apportionment of liability, rationalization, safeguarding guaranty recourse claims and traceability.

The QAA is an agreement *sui generis*⁴² with the unique characteristic of determining the supply company's organization structures in a binding contract as prerequisite for performing the contract.

A violation of organizational obligations establishes an entitlement to claim damages according to Section 280 (1) of the German Civil Code (BGB) irrespective of the right to claim damages due to defects in breach of contract relating to the product. Claims as defined by Section 280 of the German Civil Code are subject to statutory regular limitation periods and not limitation periods applying to purchase agreements under German law.

QAA are targeted at avoidance of errors in the entire value chain. The obligation to inspect purchased products is essential to performing the contract and cannot be waived. Not carrying out incoming goods inspections according to ISO/TS 16949 – 7.4.1 and 7.4.3 so as to ensure that purchased products are defect-free exposes the customer to an estoppel

⁴² Ensthaler/Gesmann-Nuissl/Müller, *ibid.*, p. 139.

under German law on grounds of severe contributory negligence as well as violation of his duty to avert or reduce damage. The supplier is hence liable towards the customer at the next level of the supply chain.

QAA is based on bilateral and corresponding obligations to communicate. Whoever does not communicate commits a breach of contract as set out in Section 280 of the German Civil Code.

Claims due to tortious acts according to Section 823 (1) and (2) as well as Section 826 of the German Civil Code may be possible.

It is not clear whether QAA can have protective consequences for third parties.

Noncompliance with QAA can compromise insurance coverage.

The QAA's consequences with respect to liability where ISO/TS 16949 is the QAA's basis cannot lead to not concluding QAA. Such action would not change the legal situation since ISO/TS 16949:2009 is an international standard of the automotive industry and thus always leads to the same results when construing contracts. It is necessary to implement the QAA by making the supplier's responsibility to ask and the customer's responsibility to response correspond to each other within the decisive communication process. Finally, QAA is a synallagmatic contract which is based on the interaction of the processes defined and required by ISO/TS 16949.