

How To

Settle Factory Claims In China More Successfully

Volume VI

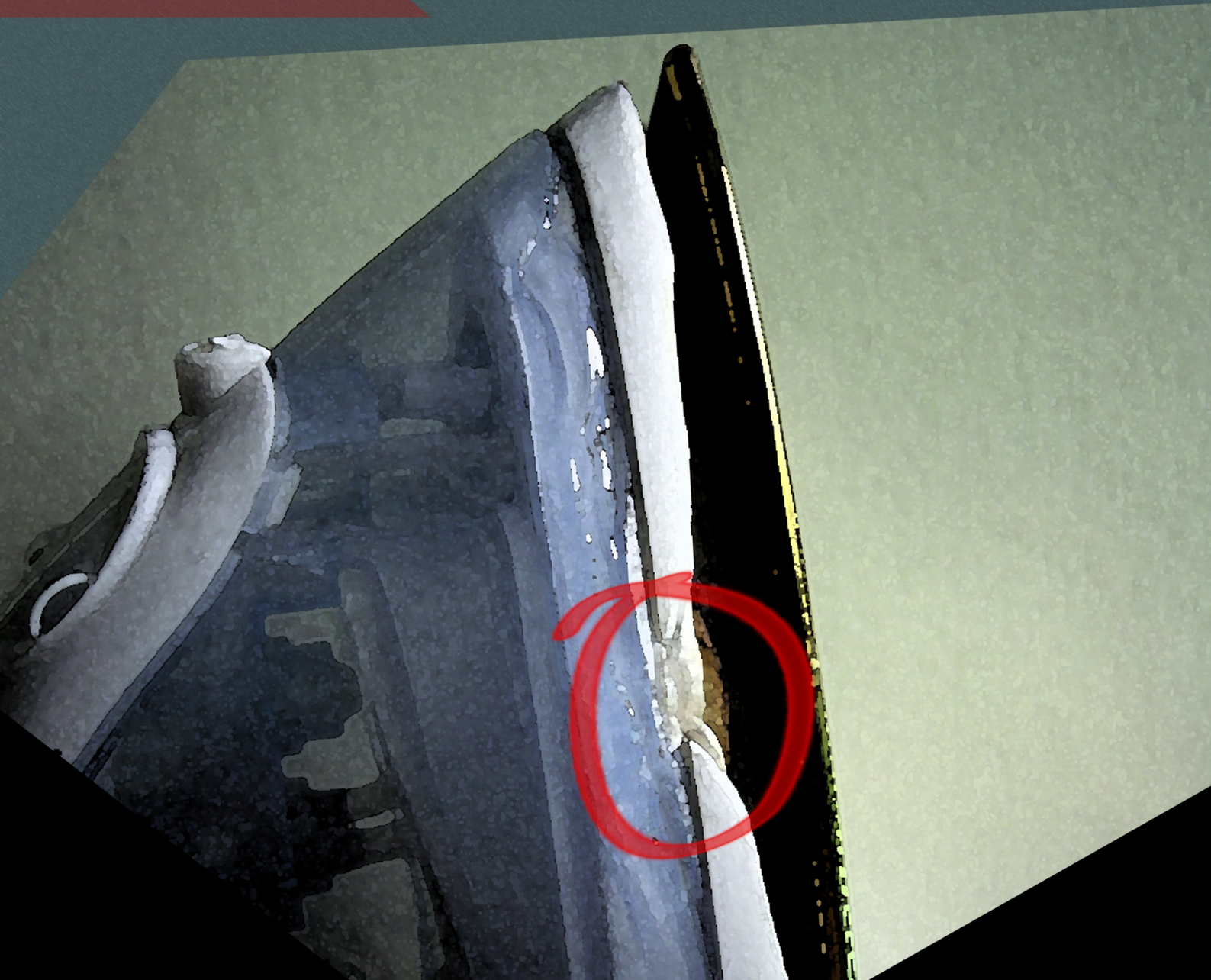


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Chapter 1 - What is a Claim Actually?

The most appropriate legal definition of a claim, applicable to importers, is “the making of a demand (asserting a claim) for money due, for property, for damages, or for enforcement of a right”. If the demand is not honored, it may result in a lawsuit.

In order to assert a right against a third party (your supplier for instance) a claim must first be filed with them. If they reject your claim, it is lawsuit time if there is no other avenue of recourse that you can pursue.

In this eBook I often use the term “Supplier” that stands for a factory, the factory’s representative office, and a trading company (agent).

This eBook assumes your company to be a small or medium size importer with an established customer base in your home country or a company interested in starting their own importing but lacking the necessary experience to do so.

Chapter 2 - What Your Company Can Do to Avoid Having to File a Claim Against One of Your Suppliers?

In light of the current legal climate, it is prudent for companies that regularly import goods from China to assess whether they have meaningful exposure to future lawsuits and, if they do, to take proactive measures now to protect themselves against, or at least limit, any future liability. Preparing for the potential rush of legal actions is a complex task requiring careful planning on several fronts.

Often overlooked by importers is that the prevention of claims starts with the selection of your suppliers in China and your own preemptive actions.

The Trade Show Scam

Let me give you an example of how it usually works. You visit one of the impressive Trade Fairs in Hong Kong, Guangzhou, Shanghai, or Ningbo and talk to as many exhibitors as possible. You come upon one company that has a nice booth, friendly staff, and one of the products you have been searching for. On top of that, their prices are much cheaper than the rest of the exhibitors.

You ask for a catalogue along with the company representative's business card and you ask them to note their price quote on the business card. Since you are in a hurry because you still want to meet many more companies that day and other businesspeople are queuing behind you, you tell the booth representative that your company will contact them as soon as you return home.

You are very happy that you had a successful day and found a new trustworthy supplier.

Unfortunately, you already made a big mistake.

Unreasonably Low Price Quotes

Never take for granted prices that are quoted to you during a Trade Fair. Especially if they are much lower than those from other suppliers. If something seems to be too good to be true, it surely will not be true.

This should certainly be applied to manufacturers in China. If one thing can be said about the Chinese people, it is that they know how to calculate prices accurately.

All you need to do is ask yourself why are the other companies unable to quote a similarly low price? Simply put, they cannot because they have calculated their prices based on their BOM (bill of material) and know exactly what their total cost is. If someone offers you a much lower price, he did either not do his homework properly or he simply is not playing fair.

The Story Unfolds

Now let's continue with the story. Back home, you proudly present your great discovery to your sales managers. Together you decide to go ahead with this terrific new product at a bargain price.

Now you have made the next big mistake. Never make a final decision before you receive proper samples from the supplier. Next, the samples must be tested and approved by your QC staff. At a minimum, the samples must comply with the legal requirements of your country. They

should also meet your own high quality standards that you give to the supplier before the samples are made.

You have probably figured out where this story is going but let's continue. Your sales managers do their jobs and begin offering the new product to your customers based on the very competitive price that was quoted to you at the Trade Fair booth.

Your company has just made another big mistake by offering something to your customers based on a quotation from an unknown supplier.

I do not want to scare you too much but during my long professional career in China, I have seen cases exactly like this over and over again.

Step 1 - In-house Quality Control

How can you make sure that your company does not become the victim of an incompetent supplier and their sales staff?

The first thing you want to do, if you have not done so already, is to establish your **own in-house quality control department**. That is the first step to making sure that your company has the means to control the quality of all incoming samples or any other quality issues before you place any purchase orders.

Alternatively, you can employ one of the existing quality control labs in your home country. The main point being that it is imperative that quality controls be in place. However, I would consider outsourcing quality control only as a temporary solution if you plan to expand your import business in the future.

It is worth noting that these labs are not shy about charging you extensively for their services. Depending on your import volume, their cost may prove simply too expensive for you to achieve the profit you are expecting.

I suggest that you only consider them for specific tests that are required by your national or local authorities. Another reasonable use is to obtain third party certificates or testimonials that you may need if you have a customer claim needing to be resolved with your China supplier.

Having your own quality control department can give your company an edge over your competitors that do not have in-house quality control capability. If your competitors already have this service and you do not, starting a quality control department will level the playing field.

Customers hate filing claims and the extra costs related to quality issues. They prefer to buy goods from a source that provides reliable quality assurance. You should consider the cost of setting up a QC department as an investment in the future of your company.

What size Quality Control Department is Best for You?

At the beginning, you do not want to start with too large of a department because you will be learning from experience. Efficiency should be more important to you than size.

The composition of your department depends very much on the nature of your import products. If you are in the textile business, you may want to hire a textile engineer plus one or two assistants. If you are in electrical or electronic products, you need to hire an electronics engineer plus one or two technicians.

To perform their quality tests properly, your specialists will need suitable technical equipment. A note of caution: do not jump the gun by establishing a fully equipped lab at this early stage. That would prove very expensive. The easiest way to determine the kind of technical equipment needed is to rely heavily on your engineers after they are hired. They will know what is needed and where to get it. A discussion about equipping the test lab can easily be included in the interview process for the engineers.

This is the most reasonable way to establish your own functioning quality control department at an affordable cost and in the least amount of time.

Step 2 - Visit Your Suppliers in China

Visiting your Chinese factories on a regular basis is a must for all importers that want to minimize their risks. As a businessperson, you regularly take precautions to protect your company's interests and visiting your suppliers' factories needs to be included as an insurance policy.

In this section, I emphasize the importance of personally visiting your suppliers in China. You may have heard other consultants that do not see the necessity of going to China at all. They suggest their clients order samples and place orders based on the results of their sample evaluation. I strongly advise you against this and will explain why. I have over 25 years of experience importing goods from China that tells me otherwise.

Of course, some very large manufacturers in China have solid QC organizations that can guarantee you a relatively constant level of quality products. If you choose one of them, you can probably afford to be a little easier going. However, chances are that they cannot offer you the most competitive prices because their superior QC organization costs money.

Also, they likely already have a customer base in your home country distributing their products. This makes it less desirable to buy from them.

Unfortunately, even the much better organized companies cannot prevent you from being forced into filing a claim. Further into the book, I have included examples of very large value claims I have successfully helped to resolve. These demonstrate that size is not everything when it comes to filing claims.

Why Visit Small and Medium Suppliers?

Most likely, you will want to deal with smaller or medium size factories. These companies need clear instructions from you and this can be only done if you sit down face to face to discuss your requirements and expectations.

Remember this eBook is about settling claims that arise when you import from China. How do you expect to achieve this without ever visiting your suppliers in person to explain and discuss your quality requirements? You need to go over designs and standards. You need to ask them pertinent questions and answer their questions to be positive they fully understand your requirements. Only after you have clearly laid out your requirements will you be in a position of strength if things go badly.

Besides, the Chinese business culture favors frequent personal contact with their overseas trading partners and visiting suppliers is the best way to do this. It will go a long way in developing a good working relationship that will pay off time and time again.

The smaller and medium size factories can usually offer you prices that are more competitive. Since you are getting into importing to improve your profit margin, they will most probably be the better partners for you.

By visiting your pre-selected factories, you will be in the best position to decide with whom you want to deal with and whom you will entrust with your precious money but only after you have concluded your negotiations.

During your factory visits, you will be in for many surprises. You may have to revise your first judgments that resulted from your earlier communication with some of the factories. You will find that some factories are smaller than expected and have less production capacity available on their premises than you had been led to believe. They do not want to miss out on your purchase orders so they asked a **subcontractor** to produce for them instead.

This is totally unacceptable because the subcontractors are almost always inferior when it comes to quality management. More importantly, they care less about your orders because you are not their direct customer. If a factory has a policy of hiring a subcontractor without informing you, simply do not work with them if you want to stay out of trouble.

Hiring a Knowledgeable Consultant

Another way that you can achieve good results is by employing a neutral outside company as your personal consultant.

Our company provides these services at an economic cost. We have a deep understanding and knowledge about importing from China based on dealing with Chinese manufacturers for more than two decades.

Once you send your requirements to us, we will execute your project in the best possible manner. You will not need to be concerned about inferior factories because our proven and experience based Due Diligence process avoids them every time.

We have no special relationship with any factory and will always follow your clear instructions. Here is the link to send your inquiries:

<http://www.webmediabiz.com/consulting.php>

Professional Audits

During your factory visit, you might ask them if they have been audited before. If the answer is yes, ask to see the audit results. This will give you an idea about the factory's performance capability.

If they have not been audited, ask their permission to have an audit conducted. Explain that a positive audit outcome is the only way you will be able to do business with them in the future.

You should ask the appointed auditing company to include a credit check of the factory. These checks usually cost less than US\$ 1,500 and they are often quite revealing. Among other things, such a check can reveal if the businessperson you are about to contract with is in fact the factory owner, or just some broker posing as the factory owner.

Does the factory pay its bills? A thriving company is far less likely to risk its reputation by cutting safety corners to save a few Yuan than a company on the verge of going under. The credit check may also reveal other Western companies to whom the Chinese company has been supplying products.

What do these other Western companies think of this Chinese supplier? Learning that a well-regarded Western company has been purchasing product from the Chinese factory without major problems for the last five years is obviously a good sign.

Trip Preparations

Visiting one or more factories is relatively easy because the factory will arrange ground transportation for you. The first factory does not even mind to delivering you to the second factory, their competitor.

Since transportation takes a lot of time, you first need to make inquiries with the factories for their exact locations. If you schedule your meetings according to their suggestions, you can save substantial time that is better spent in discussions.

It should be obvious that it makes more sense visiting your supplier at their factory rather than meeting them in your nice hotel, which would be so much more convenient. A hotel meeting deprives you from meeting the entire team you are dealing with.

Before visiting any company in China, whether a factory or a trading company, make sure that you have your business cards ready. There is really no excuse for not having enough business cards with you. In all major cities, there are print shops that can quickly print business cards for you if you run out. In the Chinese business culture, it is very unprofessional when you cannot hand out enough business cards to your negotiation partners.

It would also be unwise considering the high factory staff turn over rate. Key staff members change as they move on to other factories for better opportunities. If they have your business card, you can bet that they will contact you sooner or later. These people already know your requirements. Visiting them at their new factory could be very helpful because they will do everything to convince their management that your company is an important customer and you will receive better price quotes.

I recently read an article from another author stating: "In my experience almost every sales person that I have met in China who is not the owner of the business, has shown interest in either setting out on his own by 'stealing' his employer's customers and product designs or simply doing his own deals on the side through friends, contacts, or family."

There is some truth in that although I cannot fully endorse it or maybe I have just been lucky all these years.

On the other hand, Chinese people want to be recognized and when meeting around a conference table you can only address them with their correct name after you have received their business card. For visitors from western countries it is usually quite difficult to memorize all the different names and without their business cards, you will almost certainly fail.

If you have a notebook computer bring it along to all of your meetings. If you do not have one, consider purchasing one. Believe me, the purchase will be worth all the money you spend for it.

Your notebook computer provides you with all the information necessary to conduct business negotiations and enables you to show your company background information and your packaging concepts to factory management. You can also input information from your discussions without the need to later type your paper notes into reports. This is easier if you have a business associate along but with a bit of practice you can manage typing notes while still giving the meeting your full attention. This saves you precious time organizing information when you return home or you could even send your reports on a daily basis to your head office if further action is needed.

The Trip to the Factory

Upon arrival at the airport, it is not unusual to be greeted and escorted to the factory by both a driver and the supplier's sales manager. The company owner might even show up to greet you and ride with you to the factory. The Chinese truly are good hosts.

This is a good thing because in most cases the driver does not speak English. It is also a good opportunity to use the drive time to make some small talk with the manager. You can begin developing your first in-person impressions before the meetings and negotiations begin. Use this time to learn the position your contact holds in the management hierarchy and who makes the final decisions.

That is important because the Chinese may want to delay decisions at the conclusion of your meetings. They will tell you that they have to wait for the final decision maker who is not available now. Since your whole purpose for visiting suppliers is to make a final selection of your future business partner, you should expect the decision makers to be present so that you receive their final proposal to base your decision on.

The Factory Tour

At the factory, you will be shown around the premises. Be sure you take your time studying the production lines, their QC arrangements, and the amount of technical equipment the factory is using. Additionally, you must check whether the factory is complying with Chinese labor laws that prohibit the use of child labor and extended working hours. You will definitely want to include a clause in your P/O about labor law compliance to protect your interests. Since you are only asking the factory to comply with existing laws, there is no reason for them to object.

As you tour through the building(s), be sure you check out what is currently in production and whom it is being produced for. Sometimes management may be reluctant to disclose this information but you can learn it from packaging materials or shipping cartons.

Do not be shy about taking photos. You should ask first, but I have seldom been prevented from doing so.

Learning Their QC Processes

Look at the cleanliness and tidiness of the factory. If there is no space available to store the completed products before they are packed, you can expect that some of them will be scratched or covered with dust. Even if they clean the dust off before packing the goods, it will cause more scratches and damage.

Ask questions and investigate their QC processes. I typically begin by learning what they do when defects are discovered. Do they simply log the defect followed by reworking it or scrapping it without further action. Or do they investigate and correct the root cause of the problem?

Because of the high employee turn over rate, a common cause of defects is a new and inexperienced employee. A little additional training or even making the employee aware of the problem often corrects it.

Whether the factory has achieved ISO 9000 or ISO 9001 certification is not critically important as long as they take corrective action to improve production quality on a continuous basis.

Also, check if the factory has a decent or fully equipped lab. Of course this depends on the size of the factory and what kind of products are being manufactured.

Find out if the engineers are familiar with the regulatory requirements of your home country. This can be very important because it would be very difficult to teach them if they do not already have the necessary know how.

If you plan to import to the EC, the factory must deliver products that fully comply with the ROHS directives, otherwise you will be in deep trouble when non-compliant goods reach home. If they claim to be in compliance, ask how they can guarantee it. They should be able to provide lab certificates or for electronic products, they must be able to show you approval certificates from internationally recognized labs.

Refrain from accepting certificates from local Chinese labs because they are too difficult to verify.

Delivery Dates, Subcontractors, and Other Factory Details

Inquire from management about their delivery times during the low and peak seasons to gain a clear understanding of how long it will take to manufacture and ship your products. It would also be good to ask them about their order backlog, which will give you an indication of how the factory is doing.

If they only have a few orders, there may be a reason behind it that will be important to your final decision. If the factory does not adequately explain the reason, there is a chance that their competitor knows, which proves one more time how important it is to visit the factories in person. A trading company may have their own interests in mind and will not inform you that the factory has steadily been losing customers.

Another very important factor is whether the factory outsources part of their production. Common but critical production processes that should be

kept in-house include plastic injection molding, metal punching, painting, PCB injections, etc. If a major production process cannot be done in house, there is always a risk that they cannot properly control the subcontractor. This can result in schedule delays and quality problems.

Factories are usually very reluctant to let you visit their subcontractors and mostly for a good reason on their part. The subcontractors also work for their competitors and the factory you are visiting would rather not tempt you into investigating other companies. Of course, there can be many other reasons, labor law violations being another one.

Some companies subcontract final assembly to maintain schedule if they have over committed their own assembly line capacity. By all means, avoid this practice because you will often receive inferior goods. It defeats the purpose of selecting a factory based on a positive evaluation if your products are not really manufactured there.

Be sure to include a subcontracting clause in your P/O to protect your interests in the event a claim arises after the goods arrive at your home country. In many cases, the subcontracting factories are owned or managed by relatives. A very important Chinese business concept is called "Guanxi" which literally translates as "relationship". Family demands to help each other can overshadow your need for stable production and acceptable quality.

Unfortunately, another bad Asian business practice is to obtain a purchase order before having a full plan of how it will be manufactured. So, you believe you are ordering 100,000 pieces produced at this particular factory, but what actually happens is this factory is only able to produce 20,000 pieces. They outsource the rest of the production to four or five other factories where they are not able to control the quality and you

personally have little or no influence over what occurs at the subcontractors.

If you do not visit your factories, you will not be aware of these practices and may face serious problems later.

Since factories can use different ports of loading, you need to inquire which one is usually used. You need to know the applicable freight charges to accurately calculate your landed costs. Another reason to learn which port will be used is because some ports have only one container ship departing each week and you need this information if you are on a tight schedule. If you need to meet the Christmas sales season or have scheduled a major promotion for a new product, completing production on time but waiting an extra week for it to ship can turn into a disaster.

Also, some products can only be shipped by air freight. Notebook computers and MP3 players are typical examples. The key components of these products are ICs that fluctuate in price. At present, their prices are in constant decline. It is imperative buyers receive their goods within a short time, otherwise competitors that air freight their shipment at a later date will easily be able to sell at a price that eats up all of your profit. This makes air shipment unavoidable.

P/O Terms and Conditions

When discussing the payment terms with management, ask them for their banking details. This enables you to do a background check before you place your orders with them.

Finally, you need to negotiate the payment terms that are usually by irrevocable letter of credit at sight (L/C). This is usually the safest way to pay the factory and also allows them to obtain a bank loan to start production on time.

Never ever let the factory convince you to remit a down payment of let's say 20 or 30% of the total order value by T/T to enable them to start your production. Ask yourself why are they asking for this? There is only one reason, which is that the factory has no money and obviously no other orders. They are also probably having trouble getting a bank loan. They want you to jumpstart production with your cash. If something goes wrong, and the likelihood is rather great something will, you will lose your money and never receive a shipment.

Before you can negotiate prices with the factory, you need to inform them about your product and manufacturing specifications, quality standards, and any other terms or conditions. Failing to come to agreement first on these issues will likely result in very competitive price quotes but for a substandard quality that will cost you dearly later on.

Most important is making sure that factory management understands your specifications.

What sort of things do you need to specify? Included should be:

- Labeling
- Any special markings
- Packaging including the quality of cardboard
- Materials or components to be used
- Types and colors of paints and finishes
- Instructions in one language or several languages suitable for your clients? Instructions in Chinese do not go over well in Europe or the USA.

Many importers use the Pantone Color Chart numbers to inform the factory about their color or color combination requirements. I can tell you from my experience that the results will not be very good. Especially if

you have several factories involved that have to follow your color requirements.

It is much more practical and produces better results, when you use color chips instead. You can buy items that have the correct color in your home country and cut off some pieces of the plastic material. Always keep several reference samples for yourself and handover to each factory a piece that is a reasonable size. Reasonable does not mean a thumbnail sized one because it is not large enough for the factory to make the injection color accurately.

Also, consider the tests to be conducted during manufacturing and at completion. Do you need CE or ROHS approvals for importing electrical goods to Europe? If wood is contained in the product or the packing, are fumigation certificates required?

Protect Yourself From Copyright Infringements

Does the factory or supplier own the intellectual property rights of the product? Do not believe you can import well known international brands unless you buy them from the brand owner. Gucci, Samsung, Sony, or Philips or any owner of a well known brand certainly won't allow a Chinese supplier to sell their branded products at low prices through the back door! China is probably the world's largest source of fake or pirated goods by using well known logos and branding that are simply copies or worse, just a logo stuck on a similar looking product.

Not only will there be little or no warranty but worse, you risk serious legal action and possibly a criminal conviction if you cannot show proof of ownership of the brand name or that an agreement exists with the brand owner when you import under a brand other than your own or the

factory's. Even if it is the factory's brand, you still need to have a written agreement with them to distribute it.

Please take this very seriously and do not even consider trying to import fake goods. It would destroy your reputation at home in addition to the possible legal proceedings.

Making Your Decision

Your requested specifications set all the standards for manufacturing samples, mass production, and inspection of your goods. This should make it clear why negotiations need to be done in person by talking with the responsible managers.

By using the same procedure when negotiating with every factory you visit, you will receive information that is directly comparable for each quote. This will simplify your decision making process. Since you will visit several suppliers during your visit, you will have current impressions about each factories' performance capabilities in addition to the price quotes to make this important decision.

Two of my other eBooks titled [How to Make Business Negotiations in China More Successful](#) and [How to Make Chinese Factory Visits More Successful](#) go into detail on the subject of negotiating with the factory management. What I have provided here is a summary of that information. If you want more information, these books are available from our website and are a must read literature for all importers.

Step 3- Appointing an Inspection Company

When verifying the quality of goods imported from China you have three choices to consider.

1. Let the manufacturer perform a self inspection
2. Have someone from your company perform the inspection

3. Appoint a third party inspection agency to perform the inspection for you

Selection Considerations

If you really want to be on the safe side, I would not suggest letting any manufacturer check their own quality. It is much too risky and you will only find out after the goods have arrived at your warehouse that something is wrong and by then it is too late.

Having someone from your company conduct the inspection is actually not a bad idea but is prohibitively expensive if that person has to travel to China solely for this reason. What remains, is seeking out an experienced international inspection company with several local offices in China. Key office locations are Hong Kong, Shenzhen, Guangzhou, Shanghai, Ningbo, Xiamen, etc.

Why is that important? If an inspection company has only one office in Hong Kong (southern China) but frequently needs to inspect goods for your company in Northern China, you will be charged for their travel expenses including the cost for the accommodation. Over time, the costs add up and it really makes no sense to work with such a company. The better option is relying on inspection agencies with offices throughout China. The travel charges are much lower because the inspectors only have to travel from their nearest office to the factory. Besides, they are usually familiar with the area and may even speak the local dialect, which makes communication with the factory staff easier.

It is also obvious that they can visit your factory much faster because they are in the vicinity. This becomes important when an inspection has previously failed and the re-inspection needs to be conducted only 1 or 2 days later. Usually the factory has to pay the re-inspection charges after failing an original inspection due to it being the factory's fault. If the re-

inspection charges are too high because of extraordinary travel expenses from your inspection agency's head office, you are in for lengthy negotiations with the factory. They will argue and try to avoid the payment. In other words, the practical decision is appointing an inspection agency that already has offices near major production centers.

Inspection Frequency

Depending on the size and importance of the order, you may want to consider more than a single inspection after production is complete. You can choose from three primary inspection methods.

Initial Production Inspection (IPI)

This inspection takes place when approximately 10-20% of the total order quantity is produced. It normally covers the following criteria:

- Verification of the production schedule
- Check of raw materials
- Partially completed goods
- Finished products and the packaging
- Inspection for appearance, workmanship, color, measurements, quantity, packaging/packing details, compliance with directives etc.

This inspection method is used mostly when the order volume is very large and production needs to be closely monitored from the very beginning to assure the delivery deadline will be met.

The benefits of an Initial Production Inspection are that the status of the production can be verified at every stage. If problems are found early, there is still time to take corrective action and prevent the early problems from affecting the entire order. Since production is already in progress, you will have a clear picture of the factory's performance at that time.

During Production Inspection (DPI)

This inspection takes place when approximately 40-60% of the total order quantity is produced. It should cover the following criteria:

- Production status monitoring
- Raw materials or key component validation
- Quantity and performance checks on completed products
- On-site tests
- Finished products and their packaging
- Inspection for appearance, workmanship, color, measurements, quantity, etc.
- Verification of packaging materials and details

The benefits of a During Production Inspection are that the status of the production can again be verified at this stage. By performing this inspection, you can verify that corrections have been implemented since the Initial Production Inspection. Additionally, you will still have a chance to apply other corrective actions before the final inspection.

Final Random Inspection (FRI)

This is actually the most important of the three inspection categories. It is commonly used to safeguard the shipment when a consignment is 100% manufactured and at least 80% packed.

International sampling plans ANSI/ASQ Z1.4, ISO 1259, BS6001, GB 2828, or any client specific method will be used and a representative number of shipment samples will be randomly drawn for the visual evaluation.

It will at least cover the following criteria:

- Total quantity of finished product
- Cosmetic and workmanship check

- Measurement and on-site testing
- Performance check of completed products
- Inspection for appearance, workmanship, color, measurements, quantity, etc.
- Verification of packaging material, labeling, barcodes, shipping marks, etc.

The benefits of a Final Random Inspection are that usually the most serious defects or deviations from specifications will be detected and the shipment can be stopped at this stage if necessary. However since this inspection is already close to the actual shipment date, there is a risk that the scheduled shipment date cannot be met which could cause serious problems if the requested re-work is impossible or takes considerable time. In other words, a Final Random Inspection alone, prior to releasing a shipment, may not prevent or uncover risks that might appear at earlier stages of the production process.

It is therefore highly recommended that higher risk products be subject to greater QA intervention such as a product design review, supplier evaluation, prototype testing, and the execution of the Final Random Inspection in combination with the Initial Production Inspection and the During Production Inspection.

What the Inspection Agency Needs to Know

You now know the main inspection categories for verifying acceptable quality. But how is it done?

You must provide at least one sample together with all your specifications and requirements to the inspection company of your choice.

Since this inspection company will act on your behalf, as your savior in case of a non-compliant production, it is very obvious that you must feed them all the information you have to let them do the job. This is even more important when your product is more complex like home appliances and consumer electronic products.

Please consider that they can only follow the general inspection procedures and your specific requirements. If you do not inform the inspection agent about certain details, they will not take the necessary action and cannot be held responsible.

Below are links to the major International Inspection Companies. These are companies I have worked with over a long period of time. You can visit their websites, contact them and find out which is the most suitable for you.

Asia Pacific Inspection Hong Kong	http://www.api-hk.com/
Bureau Veritas Hong Kong	http://www.bureauveritas.com/cps
HKIC Hong Kong	http://www.hk-ic.com/
Intertek Hong Kong	http://www.intertek-labtest.com/
PRO QC Hong Kong	http://www.proqc.com/
SGS Hong Kong	http://www.hk.sgs.com/
TUV Rheinland Group China	http://www.chn.tuv.com/eng/index.jsp

Most of them have offices in other Chinese or Asian cities and will provide an excellent service to you.

Step 4 - Provide Precise Information in Your P/O, L/C, and Any Other Accompanying Documents

You have an important role to play by specifying to your supplier what you actually want. This is often underestimated by importers and must be addressed during your meetings with the factories.

It also has to be included in your P/O and should be as detailed as possible.

You may need to consult with your own technical staff in this process. If you do not do this, you might find that you receive a product that meets all your stated requirements and the applicable regulatory requirements, but which is absolutely wrong for your intended application. So, first of all, you should concentrate on specifying your needs specific to the intended use of the product.

What must be included in your Purchase Order (P/O)

Here is a summary of what I suggest you incorporate in P/Os regardless of the product type you are dealing with:

- Clear and detailed product descriptions including requested color, measurements, sizes, etc.
- Clear and detailed packaging information including barcodes and shipping marks
- Order quantity
- Delivery date
- Port or airport of loading
- Price

- Payment terms
- Spare parts or spare units if any
- Agreed defective rate
- Guarantee clause
- Indemnification clause
- Late delivery clause
- Transshipment clause
- Clause for compliance with requirements in your home country
- Information whether goods must be inspected and by whom
- A clear statement that the mass production must comply with the submitted and approved samples

However, do not overdo it. I have seen P/Os that could have been issued by lawyers and you can imagine that factories do not make the effort to employ lawyers just for the sake of checking P/Os. Remember, it is all about partnership and if you are still afraid the factory will cheat you, your factory evaluation was not thorough enough.

Here are additional comments about what must be included in your P/Os:

1. Order quantity - Should match the container loading capacity or the total quantity of products in case you want to place different products from the same factory in one container.
2. Packaging information - Very important because it is a cost for the factory and could be manipulated in their favor. For instance, there are several levels of corrugated cardboard quality. These are measured in grams per square meter. If you did not specify the weight you could end up with a 2-layer corrugated cardboard sheet that is so thin that you could easily punch a hole through it with your fist. This quality is unacceptable as a sales packaging because you cannot stack sufficient cartons on top of each other. The barcode information is also very important because the inspector

has to verify it during the inspection. If a barcode scanner cannot read the barcode properly, the product cannot be registered during checkout by the hypermarket/supermarket cashier. Companies like Wal*Mart consider this a major defect and would not allow any shipment under such conditions.

3. Spare parts or spare units - This depends on what kind of products you import. For technical products, you can negotiate 1 or 2% of free spare parts/spare units included in the buying price. The factory will of course calculate it. If these goods come without a guarantee or service agreement, you had better negotiate net prices.
4. Defective rate - Putting a clause in your P/O will help to protect your compensation claim in the event there is an epidemic of defects or overall poor product performance. It splits responsibilities between the factory and your company. Nobody can demand that production be completely without faults and defects. Therefore, it is fair enough to allow the factory a certain percentage of defects as an upper ceiling limit. You have to negotiate this and usually the factory will have some historic figures in mind. Everything exceeding this percentage will be the factory's responsibility. You may say "I will employ a good inspection company, which will help to protect my interests". That may be true but there is still a risk that something has been overlooked or a defect shows up later. You can imagine that this could become very expensive because there will be compensation claims from your customers or demands for price reductions.
5. Guarantee clause - Most countries have laws protecting the end consumer's rights and provide them with a guarantee period of anything between 1-2 years. In some cases, retailers have even extended this guarantee period by another year. Three years is a long time for some products with a limited life cycle. Because it is

a legal requirement (except the additional year offered by retailers), you must comply and protect your interests by adding a clause in your P/O. This gives you the right to ask the factory for compensation. Most factories however will not accept these clauses and you may have to negotiate to find a way around it and still protect your company's interest.

6. Indemnification clauses - This is another important clause that helps you if you become entangled in copyright claims or patent infringement claims. Unfortunately, Chinese manufacturers have a different understanding of copyright and patent infringements from western societies. They think, if they copy a successful product and apply some design modifications, it is their own design and they even go so far as to have it registered at the Beijing Patent Registry under their company name. If you ask them, you will usually hear "No problem - it is our design and we have already registered it". This will be of no help if the original designer sues you in your home country. Without an indemnification clause you would be in deep trouble and pay everything yourself.
7. Late delivery clause - This is relatively easy to understand. If your goods cannot be shipped on time due to the factory's fault, they will probably arrive too late for your customer's promotion and that can become expensive as well. You have to be careful here because sometimes it can be your own fault because you failed to give the factory needed information, documents, or approval to start or finish production on time. I cannot provide exact figures because they vary from product to product and company to company but you should at least request the factory use an express vessel at their own cost to make up the lost time. In a worst-case scenario, the factory should share or completely pay the compensation costs your customers negotiated with you. Some importers may even include a clause that asks the factory to ship

goods by air but in all these years, I have seen very few cases where this has really happened and usually factories will not agree to such a clause.

8. Clause for compliance with requirements in your home country -

This is another important clause because if the government authorities in your home country perform random checks at retail outlets, you may be in for a surprise when they find that the goods you supplied do not comply with local directives or laws. You should not assume that all factories are fully aware of all requirements in your home country. The opposite is mostly true. You, as the importer, are responsible to import only goods that comply with your countries laws and you must protect your company from damage for non-compliance by adding a clause in your P/O.

9. Information whether goods must be inspected and by whom - This

clause is easy. If you want the goods to be inspected, which I strongly recommend, then you have to inform the factory about the details. The inspection procedure was previously explained.

10. Information that mass production must comply with the submitted and approved samples -

As mentioned several times, you set the quality standard by approving the samples and must enforce it now by not allowing the factory to produce anything else. If you are lenient in this request, your efforts evaluating the samples and factory will have been a waste of time.

Your specific product requirements may deem other P/O clauses be included. For instance, the garment or textile industries differ from home appliances. In general, you are supposed to be the expert for your products and should have the knowledge to figure out any other needed clauses.

Please be aware that any P/O is only legally binding after an authorized factory representative signs it. Sometimes factories delay signing for quite some time. In that case, the best solution is calling the person in charge to ask what is going on. There could be a reason for the delay but the factory will try to change the delivery date. Therefore, act immediately rather than waiting in good faith.

Other than adding your specific terms, try to write P/Os that are easily understood and are no longer than 2-3 pages. Anything else becomes too complicated and requires too much effort on both sides to read and comprehend. You should be able to establish the P/O format one time and then copy and paste the contents for other products without starting from scratch.

Do not underestimate the importance of this section. If you make mistakes here, it usually will cost you money and respect. Therefore, it is advisable to discuss as much of your standard P/O content as possible with the factory management during your visit. Trying to enforce your requirements when later communicating from your home country will prove much more complicated.

You can also shorten the whole process by providing a copy or draft of your standard P/O to management during the meeting or have it sent in advance if you are certain that you are going to work with that factory.

Step - 5 Product Liability Insurance

Your contracts with Chinese suppliers should contain a specific provision requiring the Chinese seller to obtain and maintain sufficient product and general liability insurance with a reputable international insurance carrier in order to provide sufficient protection to the importer in the event of

defective or unsafe products. If at all possible, the importer should be named as an “Additional Name Insured” on the insurance policies.

Insurance should not be seen as a replacement for everything else explained in this chapter, but it is your backup. Insurance almost never covers more than your legal fees and out of pocket damages. It will not compensate you for time spent defending lawsuits nor will it repair your damaged reputation.

Chapter 3 - Recent Examples of Huge Claims with Chinese Factories in the USA

Each of the recent high-profile safety problems with Chinese imports to the United States were characterized by deceptive or dishonest business practices in an effort to cut costs and boost profits.

Melamine, which is toxic to animals, was blended into **pet food** to give artificially high protein readings.

Diethylene glycol, potentially lethal to humans, was substituted for its higher-cost cousin, glycerin, in the manufacture of **toothpaste**.

Tires were surreptitiously manufactured with either a minimal or **missing gum layer** needed to prevent catastrophic tread separation.

Toxic lead paint was substituted for the paint that was originally approved for popular **childrens' toys**, presumably to save money.

These are all cases where unscrupulous business practices have jeopardized the health and safety of the consumer.

The Importer has a Responsibility

You, as the importer, are responsible to take all necessary precautions to stop such dangerous goods from entering your home country.

You must minimize the likelihood of your products harming people and at the same time minimize your liability by doing everything you reasonably can to prevent problems with your imports. It is essential when you purchase products from China that you take action to ensure the safety

and quality of your products; **you cannot rely on the Chinese to always take appropriate action.** Even if the Chinese do not intentionally manufacture substandard products, they may simply be unaware of your country's regulations.

More Scrutiny of Imports

The only way to do this is to get more actively involved with a successful quality control program.

Dangerous Chinese products were entering the United States and Europe long before the Melamine pet food tainting incident hit the news. But that incident and those that quickly followed it (bad toothpaste being the most prominent) mean everyone is now on notice that these issues are real.

From now on, it will be impossible for any Western company to plead ignorance. Western companies that refuse to take proper action will increasingly be subject to severe penalties including punitive damages where they are legally available.

In other words, any Western company that does nothing to assure the safety of its Chinese imports and then steps into court claiming they had every reason to trust their Chinese supplier (based on faith alone), is likely to face real anger and major damages. Plaintiff's class action attorneys in the United States and Europe should be and are salivating.

Liability for damages caused by defective Chinese products is going to be huge and it is going to be vast and it is going to fall disproportionately on American and European companies.

The reason for this is twofold. First, it is viewed as difficult and expensive to sue Chinese manufacturers. Second, and more importantly, Chinese

courts do not give out **large damage awards**, so the result of a **tort suit** in China is not likely to be attractive to U.S. and European plaintiffs. Therefore, there will be overwhelming pressure to file such suits in the United States or in Europe, with the importer and retailer as defendants.

Such suits will likely be heard by U.S. and European courts and damages will be awarded. As I write this book, the tainted pet food cases are progressing through the US courts where more than 300 people are suing 30 different companies involved with importing the tainted pet food from China. More than US\$8 million has already been paid out and the companies have agreed to pay another US\$24 million. Each pet owner with documented veterinarian bills and burial costs is expected to receive up to \$900. Any funds left over will be donated to animal welfare groups.

Definition of Tort

A tort is an injury to one person for which the person who caused the injury is legally responsible. A tort can be intentional – for example, an angry punch in the nose – but is far more likely to result from carelessness (called “negligence”), such as riding your bicycle on the sidewalk and colliding with a pedestrian.

Chapter 4 - Quality Deterioration is a Major Problem in China

Quality deterioration is indeed a major problem in China. However, the reason why this is happening is not so much so Chinese manufacturers can rake in big profits, it is so they can survive. Many Chinese manufacturers have no profit margin whatsoever.

Economic Reality

Between currency revaluation, massive competition, tax reforms, and the end of VAT rebates (a Chinese tax), huge numbers of Chinese manufacturers are operating at a loss. They are sacrificing quality in a desperate attempt to stay alive for a few more months or years.

Some Chinese companies have gotten themselves into a desperate situation by pursuing contracts at the absolutely lowest price possible. China's manufacturers cannot continue this race to the bottom of the pricing scale and expect to survive.

At some point, they will need to shift to higher quality goods at higher profit margins. This shift is already happening in the market as a whole and I have seen individual Chinese companies make this shift as well.

More and more importers are being told by their Chinese suppliers that they cannot continue to maintain expected quality levels without price increases. Importers are well advised to listen to these suppliers and wherever possible stress quality and safety over bottom end pricing.

I have also seen importers fight a price increase when they certainly knew there was no way quality could be maintained without it.

It seems that economics is what is driving the quality deterioration right now. Just as it did when Japan and then Korea were not known not for the quality their goods, but rather for their low prices. This is not some special characteristic exclusive to the Chinese people. The economic reality is that this can be corrected. Time will tell if the Chinese can break out of this cycle of deteriorating quality. Japan and Taiwan did it and I do not see why China cannot do the same.

The Chinese Government Steps In

The Chinese Government has also intensified their efforts to ensure better quality for their exported goods.

Under the agreement reached at a two-day meeting on the safety of consumer products held Sept. 11, 2007, both the **U.S. Consumer Product Safety Commission** (CPSC) and **China's General Administration of Quality Supervision, Inspection and Quarantine** (AQSIQ) agreed to full cooperation in quality inspections in four categories: toys, fireworks, cigarette lighters, and electrical products that are exported to the United States.

The AQSIQ will strengthen their inspections on the exported products and assist CPSC in tracing hazardous products. Here is a link to the AQSIQ website for more details: <http://english.aqsiq.gov.cn/>

China has also agreed to provide the European Union with detailed quarterly reports to prove it is dealing with complaints about potentially dangerous consumer product exports.

Chapter 5 - Major Reasons for Claims Against Chinese Suppliers

There are various reasons for filing a claim against a factory but you will mainly be faced with:

1. **Late or incomplete deliveries**
2. **Major quality issues**
3. **Copyright violations**
4. **Patent infringements**
5. **Non-compliance with laws of the destination countries**

Let me give you more information about the likely background of these claims:

1. **Late or Incomplete Deliveries** claims can easily be avoided if your company exercises the necessary **due diligence** to monitor the production progress at the factory. If your factory was unable to produce the ordered quantity on time or could only supply part of it on time, you should have known this weeks ahead of time. It should not come as a surprise to you at the last minute. If this happens, it is likely your company's control systems either are not yet in place or need refinement.
2. **Major Quality Issues** are another claim that could probably have been avoided if your QC department and your inspection company had done their homework correctly. Of course, sometimes there are hidden defects that can be only discovered after products reach a certain manufacturing operation (properly operating technical products for instance). But these are the exceptions and I will give you some real examples along with other cases in chapter 14.

3. **Copyright Violations** are a worst case scenario and in general very costly. Since it is not a quality issue there are only a few precautions that you can take but believe me, they will not always prevent these claims. I have already pointed out that Chinese manufacturers have a different understanding of copyrights and from their point of view, everything looks alright. Unfortunately, it is still very common for factories to take famous brand name products and apply marginal changes in the hope that the design will be sufficiently altered to avoid copyright infringement. Most often, the design changes are not sufficient. My only advice to you is to carefully check the copyright or patent in your home country and do not rely on statements made by the factory, regardless of how convincing they may seem. You may want to contact a patent lawyer if you are in doubt. If you have the slightest doubt that your product(s) might violate copyrights, it is best to drop the products so you can enjoy a much better night's sleep.

4. **Patent Infringements** are another worse case scenario and can be even more costly than copyright violations. Patent infringements are sometimes very difficult to determine because they are at times only subtle modifications applied that can make a big difference. Trying to bypass existing patents without being an expert would be the same as playing with fire. You will be burned and will lose a lot of money on top of it. It is inevitable that you seek the help of an experienced patent attorney to avoid the many pit falls here. On the other hand, these lawyers are very expensive and you may wonder whether your effort to import a risky product (that's what bypassing existing patents is about) is worth all your time and money. The key point here again, is that you cannot simply trust what your supplier tells you. He is not familiar with the patent laws in your country and frankly, he simply does not care. That means you are all alone and

you are the one that will be held fully responsible if you import a doubtful product. The real life examples in chapter 14 include cases that clearly prove that you really cannot trust your supplier, even if you have had a long-term business relationship with him.

5. **Non-compliance with the Laws of the Destination Countries** is also a serious situation but different from points 3 and 4. You may be lucky and can prove to the authorities that their findings were wrong. If a problem does exist, it is very important that you can prove the problem did not happen through your negligence; meaning that you took all necessary precautions. What makes the case more serious is that you will be dealing with government authorities who are very powerful and can enforce a nationwide sales stop or even a recall of all distributed products. If that happens you will lose a lot of money and even more serious, your reputation as a high quality importer. Usually the government authorities will contact your customers first because that is where they will retrieve testing samples. Since your customers are distributing the non-compliant products, they will be liable. Still, you cannot escape your responsibilities because most retailers have clauses in their buying contracts that pass the liability for damages or claims related to purchased products from themselves to the importer.

Chapter 6 - Who is Informing Your Company of a Claim and What Actions Must You Take?

If you are faced with a claim, you have to consider your available options. Claims usually involve large amounts of money that have to be set aside for penalty payments, compensation payments, and/or logistical costs.

I will discuss this in context of the same sources of claims as used in the previous chapter:

1. **Late or incomplete deliveries**
2. **Major quality issues**
3. **Copyright violations**
4. **Patent infringements**
5. **Non-compliance with laws of the destination countries**

Who is informing your company about the problem?

1. **Late or Incomplete Delivery** problems will likely be detected by your own staff, the information will come from **your warehouse manager** when a shipping container arrives with **incomplete or missing quantities**. Your freight forwarder should report late deliveries to you when your goods are loaded into the container and shipped. You should have confirmed the vessel and departure date with your freight forwarder and therefore the late delivery should not come as a surprise to you. If your goods have been inspected (I hope you had followed my advice to arrange that), you would have known weeks ahead of time that the production was finished later than requested because your trusted inspection company had to book the inspection date when production was at least 80% complete.

2. **Major Quality Issues** can be identified by several different parties. The information can have come from your **own QC department** (you can congratulate your people if they detected a quality problem that slipped by your inspection company or occurred during the long ocean and land voyage) or the information could have come from **one of your customers**. Your customers may have their own QC department that found a problem that your own people did not (if that is the case, you have to be concerned with your QC department's qualifications and take immediate action to avoid a recurrence). This scenario is more serious because it jeopardizes your reputation as a high quality importer. Another possibility is that **government authorities** detected quality issues during tests that are randomly performed in all EC countries on a regular basis. Samples are purchased from various retail outlets and tested for quality, performance, and compliance with local regulations.
3. **Copyright Violations** will likely be brought to your attention by the registered copyright owner or more likely, by their legal representative or even worse by a court issuing a restraining order against your company. Usually a copyright violation will be detected as soon as your customers begin selling the products. The information could also come from your customers lawyers after the copyright owner approaches them.
4. **Patent Infringements** are reported to you in a similar way as copyright violations. Since these cases are much more complicated, the reporting party will usually employ a specialized patent attorney to represent them. A copyright violation is often easier to decide than a patent infringement because only real experts can decide whether a patent was infringed or not.

5. **Non-compliance with Laws of the Destination Countries**

usually results in you being contacted by one of the government authorities after they have detected the non-compliance during their random tests (see paragraph 2) or by one of your customers after they have been approached by the authority.

All 5 scenarios result with you being issued a written notification and there will probably be a deadline for you to reply or take action.

Which actions must you take?

1. **Late or Incomplete Delivery.** Missing quantities must be immediately reported to your supplier in China and your forwarder as well. It is unlikely that a large number of products are missing but sometimes it happens that between the factory and your warehouse, goods come up missing (are stolen). The supplier will always refer to his packing list but my experience is that if you are only missing a minor quantity, most suppliers will honor your relationship with them and compensate you for the missing goods because it is difficult to trace where the incident happened. The remedy could be shipping the missing quantities with the next container FOC (free of charge) or allowing you to deduct the value from your L/C payment. On the other hand, containers are normally sealed before shipment and it would be difficult to steal something without breaking the container seal. Missing quantities should not happen too often, otherwise it indicates something is seriously wrong within your supplier's organization. Late deliveries or partial deliveries should only be accepted by your company on a one-time exception basis, otherwise you set the standard for all future shipments because you have shown too much leniency towards your supplier. I believe that punctual delivery of each order is essential

because you have commitments to your customers. Large retailers require suppliers accept penalty clauses for late deliveries and that could become an issue here. I mentioned in chapter 2 that your P/O must contain various clauses including a **Late Delivery Clause**. This clause will now apply and there could be substantial money at stake if you missed your customer's promotion. In any case, you must file your claim with the factory and ask them how they will compensate you.

2. **Major Quality Issues.** You must immediately stop all deliveries of faulty products to any of your customers. If additional containers are on the way to you from China, the likelihood that these products will be also faulty is quite high. Inform your supplier immediately (see filing a claim in chapter 7) and negotiate with him about what to do with the remaining quantities. Your supplier usually has an interest in solving the situation quickly otherwise, he will not be paid. Be prepared for your customers to return the faulty products to you and charge you for the transportation costs. Large retailers will also deduct the value of the returned goods from their next payment to your company. So it is again about a lot of money. File your claim with your supplier as soon as possible. It is also in his interest because he may face the same problem from other customers if the problem is not solved right away.
3. **Copyright Violations** require that you comply with the deadline and inform the copyright owner of actions you have taken. Of course, you can object to his request if you are 100% sure that your products do not violate his copyright. That might be a very bold step because, in my experience, in most cases the copyright owner will have a solid case against you and you will not win. Copyright violations do not leave much room for leniency. If your

company has violated somebody's copyright and he can prove it, you will not be allowed to continue selling the products and will be issued a court restraining order to make sure that you obey. If you are lucky and this was your first delivery of the copyright goods, the requested compensation payment will be lower than if you have been importing the goods for months or years. Your company has to provide evidence of the total imported and distributed quantities to the copyright owner or his legal representatives. Bargaining over the compensation payment can take quite some time and you will have to pay lawyer's fees as well. File your claim with your factory immediately but leave the total compensation amount open, because it is not known at this stage.

4. **Patent Infringements** require that you meet the deadline to inform the patent holder about any actions you have taken. Objecting to his claim might be more difficult than objecting to a copyright violation due to the more complicated nature of these cases. It will be a lengthy process and the outcome is uncertain. In any case, you will need the help of an experienced patent lawyer. A normal lawyer will not be of much use to you because they lack the required knowledge to assist in these cases. It will again be about a large amount of money (you will find examples in chapter 14). Filing a claim with your supplier as soon as possible is essential. You will not know the total compensation amount because it will be decided later but file the claim right away.
5. **Non-compliance with Laws of the Destination Countries** again requires you to comply with any deadlines and informing the authorities of actions you have taken to solve the problem. You will likely have fines and fees to pay based on how long it takes you to resolve the problem. Failing to take prompt action will only make a

bad situation worse. Remember it is the government you are involved with and their offices are quite powerful. Once a violation is proven, they won't take "No" for an answer. Since your product has breached the law, at least that is what they will try to prove to you, anything is possible. The authorities have the right to ask for a nationwide recall of your products that could require newspaper, radio, and/or TV ads. I do not need to tell you how damaging this will be to your reputation. To be blunt, it could easily kill your company. Since all of your customers will learn about your problem, they may discontinue purchasing any of your products to avoid tainting their own image. You may ask: "How it is possible that the violation was not detected earlier"? Unfortunately, this can easily happen if you are importing technical products like electrical home appliances or consumer electronics products. Again, you will find real life examples in chapter 14. In the EC, electronic products must comply with the EMC (Electromagnetic Compatibility) law that has limits for electromagnetic emissions. Samples that are prepared for EMC approval are usually within the allowed tolerances but they may not be maintained during mass production. If your Government authorities draw a lot of five samples and the majority fail to meet the regulatory limits, your products are unfit for sale. If it is only one out of five products, your product may remain viable for sale if you can prove to the authorities that it is a one time exception and provide the authorities with a corrective action plan from your factory. In any case, you need to file a claim with your supplier immediately as part of your action plan and deadline. If you have shipped a large quantity to your customers and have to recall these quantities from them, you will need a large compensation amount to cover all your expenses.

Chapter 7 - The Claim Filing Procedure

All claims involving a substantial amount of money require sufficient evidence to back them up. In the previous chapter, I pointed out that all claims opened against your company have to be made in writing. This becomes the first piece of evidence for you to in turn present to your supplier.

What else is needed to open a proper claim against your factory in China?

This is easiest to understand is by again referring to the same five claim scenarios used in the previous chapters:

1. **Late or incomplete deliveries**
2. **Major quality issues**
3. **Copyright violations**
4. **Patent infringements**
5. **Non-compliance with laws of the destination countries**

Make sure that your information is as precise as possible and easy enough to understand that your Chinese supplier can take necessary actions. It is therefore clear that all information must be provided **in English** or even better, when a Chinese translation can be provided. Any other language is unacceptable because your Chinese supplier may already have enough difficulties following your English explanations and bringing in a third language just confuses things. I have often seen documents in German, French, or Spanish that were simply attached to the communication in the hope that the other party will somehow manage to understand it.

Considering the amount of money involved in these cases, the cost for a translation is peanuts and should not be objected to by management.

1. **Late or Incomplete Deliveries** claims that involve missing quantities in a sealed container should include photos of the partially empty container. Your warehouse manager needs to prepare a declaration stating the quantities missing from the container and/or any export cartons that are also missing. That is usually enough because as I mentioned before, it is very likely that the missing quantity is a relatively small amount. That does not mean that you should close your eyes and forget about it because otherwise the missing quantities might increase during future shipments. If you want to file claim that your factory made a late delivery it will mostly be about penalty payments for late or non-delivery to your customers. Since larger retailers have standing procedures for these situations, you can compose your compensation request simply by specifying the amount that you had to pay to your customer. It could be everything from lost profit, to a fixed amount per customer outlet, to the difference between your selling price and the selling price of one of your competitors that your customer had to purchase a substitute product from and even the cost of printing promotional leaflets or newspaper ads. The list can go on but the result will always be a substantial amount of your hard earned money. Earlier, I mentioned that late deliveries can be avoided by closely monitoring the production progress. It would have saved you a lot of money and trouble if you or another company representative would have visited your factory and verified the progress on the spot. Alternatively, you could have appointed a **consultant you have confidence in**, like our company <http://www.webmediabiz.com/consulting.php>, to perform the oversight on your behalf. Your expenses for these services would be a fraction of the compensation requests from your customers. If your supplier signed your P/O and confirmed the delivery date,

thereby accepting your late delivery clause, you will have enough evidence to substantiate your case.

2. **Major Quality Issues** require that you find a solution for any outstanding shipments that you cannot and should not accept because they will only multiply your problems. Most importantly, you have to provide adequate evidence to the factory that supports your claim. Suppliers usually do not like self-declarations regarding quality issues because they could be manipulated or be an underhanded way of returning goods the importer found difficult to sell. You will probably need outside help from one of the internationally accredited labs in your field. Suppliers will always argue that the products passed the inspection and they are therefore not liable because the inspection report is evidence that their quality was acceptable. Do not fall into that trap. Anything is possible from a bribed or deceived inspector to poor workmanship or packaging that affected the product quality during the long sea voyage. If government authorities confirmed major quality issues, you will have their evidence to present to your supplier. Your claim must include the transportation charges that your customers will back charge to you. Major quality issues mean that part of your turnover and invested money is tied up in defective products that are also occupying valuable storage space in your warehouse. Therefore, a prompt solution is needed. A possible solution that your supplier may agree to is paying to have the defective goods reworked in your country. A problem probably lies in the much higher labor costs of your country, which your supplier will object to. I suggest that you seek a compromise that will allow you to resume distributing the goods in a relatively short amount of time compared to sending the goods back to the factory for rework. The

Chinese Government sometimes restricts the return of a larger number of goods to China so you may be stuck with them anyway.

3. **Copyright Violation** claims require that you first provide all evidence to your supplier. That should be relatively easy since you have received sufficient information from the copyright owner or their legal representatives. In most cases, you will not be allowed to continue selling products that violate copyrights in your home country. However, the copyright may not cover every country in Europe or the Americas and there is a chance that you can get rid of the goods by selling them to a customer in countries where the copyright is not registered. Of course, this will only be possible if you substantially reduce your selling price. It is however, an option that you should not overlook because you will receive the majority of your money back and can prove to the copyright owner that the claim has been resolved. Naturally, you will file a claim against your supplier for all unrecovered expenses. He will most likely accept them because returning the goods to his factory would be even more costly. If this solution does not work, there are not many options left. One is to destroy all of the goods and file a claim for compensation from your supplier. Another is returning all of the goods to your Chinese supplier. I believe it is next to impossible to obtain compensation from your supplier after all the goods have been destroyed in your home country. It is better to return the goods to China because your supplier may find a way to sell these goods to other countries at a discount price helping to reduce his loss. If you do not mind if your branded products are later sold in some African or Middle East countries, you may want to accept this solution. Remember, your company has to provide evidence of the total imported and distributed quantities to the copyright owner or his legal representatives. They may want to claim a per piece

compensation either from all the imported goods or all the sold and distributed goods. You may try negotiating a lower value but you cannot totally escape making a compensation payment. Evidence of your compensation payment to the copyright owner must be presented to your supplier in expectation that he will refund the amount to you.

4. **Patent Infringement** cases are often solved by negotiating a royalty payment per item. The patent holder and his legal representatives will provide you with all necessary evidence to make your claim against the supplier. These are often lengthy and costly cases. Once you come to agreement with the patent holder and pay the required compensation, you will be allowed to continue your sales activities. All other details are similar to cases described in the copyright violation section and require you to take the same actions.
5. **Non-compliance with Laws of the Destination Country** cases also require that you immediately forward to your supplier sufficient evidence provided by your government authorities along with your claim notice. Since it comes from an official government organization, it is hard evidence supporting your claim against the factory. Factories fear being blacklisted from selling to important economic regions, as is the case with the United States and the EC. A blacklisting would deprive them of a very large portion of their market and you can bet that they will do everything to avoid it. You should also know that the Chinese Government has a strong interest in not sustaining a reputation tainted by poor quality and dangerous product exports. I know of one case in which a factory producing electric irons was completely shut down for several weeks after a consumer in Greece was killed by one of their defective

steam irons. Fortunately, things have changed for the better in China and factories know that they endanger their very existence if they do not promptly respond to justified customer claims in an appropriate manner.

Chapter 8 - Business Trip Preparations

Thorough trip preparations will help make your China business trip more successful. What are thorough trip preparations then?

The most important part is booking an appointment with the supplier's senior decision maker, whom you may not have met before because you have always worked with the factory's sales manager. You need to know his full name, his direct e-mail address, and if possible his cell phone number.

If this person is not available during your planned trip, you should reschedule the trip itinerary to assure meeting with the right person. Be aware that sometimes, senior decision makers intentionally make themselves unavailable for claim negotiations. Their staff may pretend that they are on an overseas business trip and you have no way of knowing if it is true or not.

Try being flexible when planning your schedule to accommodate their schedule but also be strict about insisting you will only meet with the senior decision maker and no one else.

Do not get me wrong, you may first have to talk to some senior manager to initially present your case but for the critical negotiations, the top decision maker must attend. Otherwise, there will be no resolution during your trip and anything can happen after you return home.

The main reason for your trip (which you may not have been able to plan in advance) will be negotiating with your supplier for a solution to your claim. You might be lucky and get your claim resolved without traveling to China or have a consultant do it for you. These are indeed options but it is

very likely that you will need to come in person to present your case to the supplier.

Is the Power On?

Many importers do not know the Chinese Government has imposed restrictions on the use of electric power for production. In many cities, factories will not have electrical power one or two days each week. Of course, the electrical power is not completely cut off but severe penalties are imposed if the factory is caught disobeying the government's instructions. Many factories have purchased electrical power generators to overcome the power shortages. The generators run on diesel and everyone knows how expensive this has become recently. Some factories do not want to absorb the additional cost so they stop production during the electrical shut down period. Without constant communication, you may not know about it.

Business Cards are Critical!

They are lightweight and can be used long after your visit to China so bring considerably more than you would normally think is necessary. In China, everybody expects you to give them at least one business card and if you are meeting with several people, you may handout a dozen or more at a time.

Sometimes manufacturers are reluctant to provide detailed information to somebody who "is naked" meaning "being without business cards".

If you miscalculate and run out of them, you can use one of the print shops nearby to print them for you within a couple of hours.

The Chinese perform a small ceremony when exchanging business cards. Make sure to hand over and receive business cards in the typical Chinese way, which is with both hands.

If you are sitting around the table, it is a good idea **not** to put their cards in one of your suit pockets after they are handed to you. This is extremely impolite and indicates that you do not care for the person that passed you his/her business card. The proper way is to study them first (pretending to do so is OK) and place them in hierarchical order on the table in front of you.

How do you know who is the highest ranking person at the meeting? It is usually the first person introduced to you and this person is not necessarily able to speak English. It is proper to exchange business cards with that person first. In Chinese business culture, this gives him the face he deserves. This applies even if the sales manager will be the person you are in constant contact with following the visit.

It is a good practice to write a person's title on their business card if it is not preprinted on the card. Otherwise, you may find it impossible to figure out later. A person's title printed on the business card is sometimes a little bit vague and you should ask to get it right. Also, you will not be able to distinguish whether it is a male or female name. Make a note of this for future reference. It might surprise you to learn even the Chinese will not immediately know whether the name on the business card is from a woman or a man. There are so many different areas in China with special local names that Chinese from other provinces may not be able to differentiate gender by name. Therefore, add Mr. or Mrs. on the business card to make sure that it will not be forgotten.

You should also know that a person with the name **YUEN** Kai Shun is not Mr. Shun but is **Mr. Yuen** because the family name is always the first of the traditional three Chinese names shown on any business card.

However, in Hong Kong people have adjusted after a 150 years of colonial rule by England. There they mostly mention their Christian name first and then their Chinese family names, for instance **Peter Kwok**.

You Will Need a Digital Camera

A digital camera is one of the most important tools you will need during your visit. You will have many opportunities to shoot photos of products, production operations, and quality control operations. These will include close-up photos of details that cannot be seen in a catalogue.

During your guided tour of the factory premises many photos can be taken. Important examples include the working conditions on the conveyor belt and any special equipment you are not familiar with or that differs from other factories.

Especially during claim negotiations, suppliers may present you with new proposals or improvements that have already been implemented and you will need to photograph them as evidence to take home.

You can and should take photos of any unique new products that some of the suppliers will show to you in the mock-up stage. It may only be a mock-up but in just a few weeks the tooling will be complete and plastic injection can start. You should always be on the lookout for new products that interest your homeland customers. Feeding them this important information can lead to a big sale.

Another way a digital camera comes in handy: Chinese people love to take photos and love if photos are taken of them alone or with their

customers. Also, having photos of the people you met during the factory visit helps you remember who they are and what their title is. People always like being remembered when meeting a second time.

Do not forget to bring a spare battery with you because you probably will not have a chance to recharge the battery while traveling between factories. You may also need another memory card if you do not already have one of those 2-5 GB cards in your digital camera. Another way is to upload your photos to your notebook computer on daily basis. In that case one memory card will probably be sufficient.

You Need a Notebook Computer

If you have a notebook computer, bring it to every meeting. If you do not have one, consider purchasing one. That purchase will be worth the money you spend for it. Your notebook provides you with the necessary information for your business negotiations, plus it allows you to show background information about your company, and the packaging concept for your products. This is all very helpful to factory management.

Of course, you can input vital information during your discussions without the need to take hand written notes. That is made easier if you have an associate along but with a bit of practice you can manage it alone. It is also so much more convenient than using a paper notebook. I have experienced and appreciate the changes that have occurred over the last few years.

1. Before, people wrote everything on paper, the notes were then passed to their secretary for typing after returning from their business trip. Only then could the information be distributed to all the people needing it. You can imagine that it took at least 4

precious weeks from the start of your business trip until everything was completed.

2. Some people wrote everything on paper and in the evening dictated the content into a small micro cassette recorder. Their secretary at home would then type it and distribute it to the people that needed it. You can imagine that it took 2-3 precious weeks from the start of your business trip until everything was completed. Alternatively, the micro cassettes could be sent by courier service, which saved some time.
3. Nowadays, people type their vital information into their notebook computer and send it together with the matching photos at the end of each day to the head office. In that way, colleagues at home can interact and ask for additional information if something important was missed. Upon returning home from your business trip, everything should be ready for further processing and decision making.

I suggest a large capacity battery for your notebook computer. One that lasts up to 6 hours. If this battery type is not available for your model, bring another fully charged battery along. When you have meetings away from the hotel, you will find that there is not always an electrical socket nearby to connect to your AC adapter.

Sometimes suppliers will also pass you data on a memory stick (photos, line drawings, product descriptions, etc.) that you can immediately download to your computer.

That is especially important if it is a new development and no samples or catalogs will be available for some time.

Remember, the most up to date information it is what you want to obtain during your factory visits.

You Need a Briefcase on Wheels

If you are not into weight lifting for exercise, you had better bring a large briefcase on wheels.

It is torture trying to carry your heavy briefcase all day long (with your notebook computer, catalogs, notebooks etc.). Catalogs collected during your factory visits weigh a lot and you will be exhausted half way through the day from carrying them.

Your Company's Catalog

If you have your own company catalogs, bring a few sets along with you for the meetings with key suppliers. You do not have to carry them all with you but have at least one set to show to your suppliers during your meetings.

From my experience, it makes a good impression and helps to cement the relationship with your supplier if you hand over one set during the most important meetings.

Remember you are your company's ambassador and want to show your company in the best possible light.

Your Corporate Identity Artwork Concept

Creating your own corporate identity concept is very important. After spending a lot of effort on it at home, it would be a very good idea to bring it along with you to show it to the suppliers during your meetings. It

enhances the impression you make and helps suppliers better understand your needs.

Don't be surprised if the sales manager or even the company owner meets you at the airport or hotel. This is a good thing because the driver in most cases is not capable of speaking English and you can and should use the time it takes getting to the factory for some small talk with the manager. In this way you gain a first impression with whom you are dealing before the more serious negotiations start.

Try to learn the position your contact person occupies in the management hierarchy, along with who is in control of the factory, and who makes final decisions. This is important because the Chinese may want to delay decisions and will tell you that they have to wait for the decision maker who is not available. Since the whole concept of visiting the factories is to reach your final conclusion about who will be selected as your business partner in future, it is understandable that you need to talk to competent decision makers and not middle managers.

Of course, bring all documents, lab test reports, and samples that you will need for your claim settlement negotiations.

It is essential that you have all evidence with you supporting your claim against the factory. Usually the only way to negotiate an acceptable claim settlement is by convincing them that the claim is related to their negligence. Your evidence must be strong because no factory will voluntarily accept the blame without a fight, especially if it involves a large amount of money.

Samples showing the defect, or in the case of a copyright violation, the original sample from the brand name owner helps considerably to turn the

case in your favor. Sometimes you may need a dozen samples just to prove your case and to demonstrate the defect in a convincing manner. In chapter 14 you will find examples supporting this theory.

It is only common sense that your whole company must support your claim and your business trip, preparing everything that can help to recover all or at least most of your expenses.

Copies of signed P/Os or any other documents proving that your supplier accepted your terms should be brought along. You can be fairly sure that your factory will have all their documents ready, which they believe can prove that they are not to blame and that the entire fault lays with your company. Even a supplier with whom you had a good relationship may completely change their attitude when you demand a large compensation payment from them.

Chapter 9 - Visit Your Supplier in China

Visiting one or more factories is relatively easy because they will arrange transportation for you and do not even mind taking you to their competitor.

Since the transportation takes a lot of time, you are well advised to make enquiries first with your factories for their exact locations. If you set your schedule according to their suggestions, you can save substantial time, which is better spent in discussions.

Driving to the Factory

If the sales manager or the company owner meets you at the airport or hotel, use the opportunity to gain a first impression with whom you are dealing before the more serious negotiations start.

Use the time to make small talk with the manager. It is an informal opportunity to get an impression about what the supplier thinks of your claim. You may learn useful information that alters your strategy when official negotiations begin with the decision makers.

Factory Tours

After arriving at the factory, you will be shown around the premises. Be sure to take your time studying the production lines, their QC arrangements, and the amount of technical equipment the factory is using, even if you have visited before. It is important that negotiations take place in a good atmosphere and giving the factory more face by taking the company tour is certainly a positive aspect.

When the factory manager walks you through the building(s), you should check out what is in production currently and who the customer is. Ask to

see packing materials or shipping samples. These give you a clue about who else is buying from that factory. Sometimes factory management may be reluctant to disclose that information but they cannot stop their production to prevent you from seeing it. This maybe important if you cannot reach a satisfactory settlement early. Contacting another customer of the factory could give you some extra information for your case.

Engineers and Laboratories

Also, check whether the factory has a decent or fully equipped lab. Of course, this depends of the factory size and the kind of products they are producing. Check whether their engineers are familiar with your home country requirements. This is a must because it would be very difficult to teach them if they do not already have the necessary know how.

Work Load and Subcontractors

If they do not have many orders, there should be an understandable reason. Good or bad, it is important for your decision-making. If the factory will not tell you, there is a chance that their competitors know which proves one more time how important it is to visit the factories in person. A middleman may have his own interest in mind and would not inform you.

If your claim originates at one or more of your supplier's subcontractor factories (if you had allowed them to use them for your production) you must also insist on visiting them. They maybe the source of all the problems and your factory may be trying to hide it.

Factories are usually very reluctant to let you visit their subcontractors and for good reason. They work for other factories as well and the managers do not want to introduce you to competitors you are not currently considering.

Chapter 10 - Employ a Local Consultant for Assistance

When negotiating with your supplier you will need all of the professional help you can get from a trusted company. The ideal solution could be to obtain the help of a local consultant familiar with your kind of business.

This is a way for your company to gain necessary insider knowledge to turn the negotiations with the factory in your favor. Consultants have many years of experience dealing with Chinese companies and negotiating claims is part of it.

As mentioned several times, we can provide this service and have more than 20 years of working and negotiating experience in China.

It is important that you only employ an outside company that has no relationship with your factory whatsoever.

If such a company can turn the negotiations in your favor and you successfully obtain most of your demands, the money for a consultant will have been wisely spent.

Chapter 11 - Hire a Local Interpreter for Your Negotiations

Besides employing a consultant, it is advisable to bring a Chinese interpreter along with you to the claim settlement negotiations because your interpreter is key to successful communication.

This is especially true if you are trying to solve existing problems or have another reason to talk directly to the factory's engineers. You may decide to bypass the factory's English speaking sales manager because he is not be able to translate your requests adequately or may be unwilling to do so in order to protect his own interests.

It will also give your negotiations more weight if you can talk directly to the decision maker who could be the factory owner or one of the majority shareholders with the help of an independent interpreter.

The interpreter should be a neutral person without any direct interest in your business activities.

Tips When Working With a Chinese Interpreter

Here are some helpful tips that you should observe when working with a Chinese interpreter:

- Familiarity with the subject matter is highly important. Try to make sure that your interpreter is familiar and comfortable with the topic or subject being covered. Always ensure that your interpreter has a copy of the any planned speech or talk you will be delivering. Every company and industry has its own specialized language, terms, and even jargon. Interpreters may not necessarily be familiar with this before working with your company. Make sure that interpreters are given a selection of any printed materials in both languages that

they can study prior to the event. Technical materials can be especially important. Inform them about any complicated words or terminology and inquire how familiar they are with the meanings. Prepare them to deal with any tricky subjects or issues so that they can deliver with ease.

- Time management is crucial so plan your time carefully. Remember the conversation will be twice as long. A forty minute speaking slot with consecutive interpretation leaves time for a twenty-minute speech. A twenty minute Q&A with consecutive interpretation is really a ten-minute Q&A. And so on.
- Never do a rush job; always speak slowly and clearly. If you are stressed or rushing, it will affect the quality of the translation.
- The interpreter is there simply to translate what is being said and must never attempt to translate emotion. If the speaker is happy or annoyed for example, then this will be apparent through his/her body language and tone of voice.
- An interpreter must never undermine your position by answering questions on your behalf without consulting you. Even if the response is very simple or predictable they must always convey the question to you first.
- Don't be surprised if the interpretation isn't totally exact. Interpretation is not an exact science, especially if it is a "live" process. An interpreter at an event, who can see facial expressions and sense the atmosphere of an event, might translate differently than someone working from a written transcript of an event. Fast speakers may also find that details get filtered out in favor of a few key points. Although interpretation is inexact, you do have the right to demand accuracy. Do not work with an interpreter who is error prone or introduces their own bias or ideas into the interpretation. Also, pay close attention to see what you can do to make the

interpretation work successful. If the interpreter seems stuck on a particular point, ask for clarification and try restating the information in a different way. Often an example can help clarify a confusing point.

- Never assume the audience doesn't speak your language. Just because you are working with an interpreter, do not assume no one in the audience speaks English, Spanish, Japanese, and German, etc. Many Chinese people, especially in professional circles, understand English or one of the other major languages. They may understand it much better than they can speak it. Even when working with an interpreter, assume that the audience understands you.

Here are two links to Chinese interpreter services. You can contact them to find out which of them is most suitable for your specific requirements.

<http://www.tepson.com/>

<http://www.interpreter.chn.biz/>

Chapter 12 - With Whom Should You Negotiate at the Factory?

Talking to the right or wrong person in your supplier's hierarchy can be the key for successful or failed negotiations.

I can only advise you to go right to the top decision maker. That means you must talk to the company owner. This can be several people if it is shareholder owned company. You may need to meet with the chairman of the board, the chief executive, or the president. I think you get the point that your negotiations partner should not be the sales manager or a lower member of the staff. They may help prepare the meeting and assist their boss but their help is limited if they cannot make a final decision.

It may prove difficult to get directly in touch with the supplier's decision maker because they are usually shielded by their staff. Knowing the background of your supplier is essential to pinpointing the right person if your supplier has thousands of employees.

It may pay off now, if you visited that supplier before and already know the company hierarchy.

I have discovered on various occasions that decision makers in China go into hiding and cannot be reached by your company when there is a major claim. This might seem strange but if you do not nail down an appointment with your supplier's decision maker, you may end up talking to the people that shield him and end up just wasting more time and money.

Chapter 13 - Advice for Claim Settlement Negotiations

Here I will share information with you about claim settlement negotiations based on my long working experience with Chinese suppliers.

What is the Best Start Time for Negotiations?

The decision maker needs sufficient time to prepare for the meeting. Therefore, a very early start of the meeting would not be appropriate. Starting at 10:00AM would be alright in the morning and 2:00-2:30PM in the afternoon.

You don't want to have a disgruntled meeting partner for your negotiations.

Lunch or Dinner Should be Included

By all means, have either a lunch or dinner included in your meeting plan. You and the supplier have to eat and it will give you a good chance to continue the meeting in a more relaxed way.

I was once working for a Chinese/Japanese company in Hong Kong and whenever some problems had to be discussed, our meeting partners purposely showed up in the late afternoon to settle the problem and seal the deal during a dinner.

Start with Small Talk

Westerners tend to jump right into the middle of a problem. If you want successful negotiations, do not do it even if you are under pressure to solve the claim quickly. It could take 2-3 days of interrupted negotiations before a solution is found. Talk about your company first and let the decision maker talk about his achievements. If you have met with the senior manager several times, you can shorten this process. In general,

Chinese people like to know about your background and this meeting is a good way to present you and your company in the best possible way. It may help your supplier to reconsider his position by learning that you are not a bad person after all.

If you have a nice new company catalogue, this would be the time to provide a copy to your supplier.

Presenting the Facts

After the small talk, it is time to get down to hard business. **Present all necessary evidence (e.g. documents, statements, invoices and samples) to your supplier.** Present everything that you have to the decision maker to convince him of his responsibility and hopefully he will accept fault.

Samples of a defective product are especially effective at proving your case because they can be handed over and everybody can directly see the problem.

A nicely prepared folder or binder containing all of the documents and photos can help you in your presentation (perhaps several copies for the other managers as well). It would be great if you have a Chinese translation prepared for the non-English speaking members of the management team. On the other hand, if you bring an interpreter along with for the meeting, this will be his time to present your evidence.

Consequences the Claim will have for Your Company

Clearly point out to your supplier the consequences the claim has already had on your company (e.g. loss of turnover, loss of customer confidence, loss of reputation as a quality importer). Additionally you should explain future consequences this claim will have if it is not solved soon. Never

assume the supplier knows these things. He may understand little about how business is conducted in your home country.

Listen to Your Supplier's Arguments

Although you may be frustrated and even angry with your supplier, you are well advised to listen to his arguments before making demands.

Remember he is in control of a large organization, often much larger than your own company, and deserves some respect. He will likely try rejecting your claim but you still must listen to him before proposing a settlement.

Line out Your Settlement Proposal

Lining out the details of your settlement proposal is very important. If something is unclear or misunderstood, this is the time to straighten it out. Usually suppliers will ask for a written copy of your proposed settlement to review before the meeting. There is nothing wrong with this but a personal presentation gives it more weight.

Listen to Your Supplier's Reply

Your supplier has to reply to your proposal and now he may have new ideas for solving the problem. Be patient if you want to achieve anything. You came to solve the claim and must be willing to invest sufficient time.

Give Your Supplier Time to Reconsider

It is very unlikely that your claim will be settled on the first attempt. It may be necessary to give your supplier some extra time to consider all the information presented and the proposed settlement. He also may want to investigate details within his company or seek outside advice.

It would be perfect timing if it were time for lunch or dinner. Take a break from the serious discussions and have a meal with your supplier. They

may try to ply you with some heavy drinking but that is part of the game. Join in if you want. It may lead to an easier resolution of the problem.

Another Meeting and Hopefully a Revised Proposal

During the next meeting, which could be within the next one or two days, listen carefully to any revised proposals your supplier comes back with.

Most likely they will propose some solution if your arguments and evidence were sufficient. If they still reject your claim or insist on a previous proposal, you may have to take a tougher approach by insisting a new proposal be put on the table.

Show Your Willingness to Compromise

Never let the negotiations get out of control. I will give you an example that earned me the respect of the company owner.

I had a meeting in China with one of our audio factories because they wanted to delay all of our orders for weeks and months and we needed the goods urgently for our customers' promotions during the peak season.

After several hours of unsuccessful negotiations at the factory, they switched off the lights (around 6:00PM) and told me that they and their workers had to go for dinner now. They expected me to leave, since I was not invited for dinner. Instead of leaving, I just kept sitting and forced the company owner to continue with our negotiations and later that evening we found an acceptable compromise.

I had no choice but to be persistent because our company had a large booth at the Berlin Consumer Electronics Fair and our company owner needed to inform our customers the outcome of my negotiations.

I want to emphasize again, reserve enough time for the negotiations. You will not be back in China soon and you need a resolution before you leave.

Calculate the Losses

It is very unlikely that you will recover all of your costs. If your supplier offers a compromise, you have to do the math again to determine if the result is acceptable for you. If their proposal is insufficient, make another counter proposal or request a time for another meeting to bring back a counter proposal. However, this only makes sense if you have the feeling it will help to improve the outcome.

If you feel that the supplier will not be open to an improved offer, you might as well make a decision now whether you want to continue meeting or accept their current offer.

You have another option that can be taken immediately. It is visiting other suppliers in the area. There is more detail on this subject in chapter 23.

Talking to other suppliers now can have one of two possible outcomes:

1. You let the supplier that you have a claim against know that you will be meeting with other suppliers before the next meeting.
This applies more pressure on your existing supplier to bring back an acceptable settlement
2. You want to move your production to other suppliers and terminate the arrangement with your existing supplier

Terminating the arrangement with your existing supplier should only be done as a last resort because it is very unlikely that they will voluntarily compensate your company for anything at that point.

Sometimes it still may be helpful because it sends a signal to other suppliers that nobody can push you around.

Chapter 14 - Examples of Real Life Claims

These real life cases may help you make better decisions during claim settlement negotiations with a factory.

Case 1 – The Broken Glass Carafe

A Coffee Maker's Glass Carafe breaks during operation. This is an example of major quality issue. It is also a typical example of quality deterioration by Chinese manufacturers.

Over about a 5-year period, our company purchased large quantities of a simple 10-cup coffee maker with a glass carafe. The total quantity exceeded 800K and we had no major quality problems with the product during that time. For that reason, it was decided to skip inspections in order to cut costs and maintain our competitive price.

Suddenly our customers began reporting a serious quality problem. The first time the coffee maker was used the glass carafe would break shortly after the machine was turned on.

Our customers returned all of the coffee makers to our warehouse and asked for replacements. Since that coffee maker had been distributed for a long time without any problems, the question needing an answer was what caused the unexpected problem?

Making the situation worse, several additional containers were already on the way from the Far East and our factory had produced additional quantities for future deliveries. By the time they were all counted, we had approximately 50K coffeemakers in our warehouse including those returned by customers.

We performed tests in our own lab that unfortunately confirmed our customers' findings. In search of a fast solution for the problem, I went with one of our engineers and an interpreter to our supplier's factory in China.

The case was even more complicated because we had been forced to buy the coffee makers through an export company because the manufacturer did not want to be directly involved with customers.

Of course, we filed our claim with the factory as soon as we became aware of the problem. The company owner showed zero cooperation and only briefly attended the meeting. He argued that they had not changed anything on the coffeemaker and rejected our claim.

We continued discussions with the vice president and some engineers. Our suspicion was that the manufacturer had exchanged the glass carafe for a cheaper and less heat resistant one to save costs. After the owner's denial of this, it appeared not to be the situation. We did not reach a conclusion during that first meeting and decided to arrange another meeting after we had retrieved more samples from our head office.

After we received 20 samples from our head office, we again performed tests on few samples to confirm the problem was real.

During the next meeting at our supplier's factory, we asked their engineers to test our samples under normal conditions (full water tank, paper filter, and coffee grounds). One by one, the glass carafes broke during the first minutes of operation, proving our case.

Additionally we drew samples from the completed production in the factory's warehouse. After our German customers informed us about the

problem, we had immediately stopped any further shipments, leaving us with an unlimited supply for further tests at the factory.

All tests confirmed the quality problem but nobody knew the cause of it. Once we had the factory's attention, they spent extensive time investigating the problem.

We sent samples of the glass carafes to an internationally accredited lab in Hong Kong to verify the quality of the glass. The result that came back was the glass met the required quality standard but was at the lower end of the standard.

I visited the factory in China at least 3 more times and our engineer was there 2 more times. I point this out because factory claims usually cannot be solved in one day. Especially when technical issues have to be confirmed before any compensation negotiation can take place.

After various tests, the factory was able to determine the problem was created by a very small plastic valve (cost approximately US\$ 0.05!!!) that did not work properly. It caused a slightly delayed water flow that allowed the glass carafe to heat up to a temperature that exceeded the temperature limit for that quality of glass. If the water flow had started on time, the water would have cooled the glass enough to prevent it from breaking.

Solving that problem would be very expensive because of the large quantities of defective coffeemakers in our warehouse in Germany.

At another meeting at our hotel that took place during the Guangzhou Trade Fair, we managed to come to agreement. The factory would send 50K higher quality glass carafes to our warehouse in Germany free of

charge. Additionally the factory would change the faulty valve in all the coffeemakers still at the factory and a tight inspection was performed on the quantity before shipment.

Conclusion of the case:

1. The customers were right with their claim
2. We were negligent by not performing an inspection
3. The factory was at first uncooperative
4. Presenting the evidence in person convinced them
5. Replacing the poor quality glass carafes with better ones avoided repairing 50K coffeemakers without affecting the end user
6. We avoided a costly return shipment and time consuming rework at the factory
7. We could continue our sales after the better quality glass carafes arrived at our warehouse and after receiving the reworked coffeemakers from the factory

Was it a good solution? Considering that the supplier rejected the claim at the beginning of the negotiations and that the factory was not our direct supplier (goods were exported by an export company) it was an acceptable solution. We did not recover the transportation charges that our customers had debited from us and also we could not recover any compensation for all our troubles.

As you can see, even after 5 years of cooperation and more than 800K purchased coffee makers, the factory owner did not fully cooperate and had to be convinced that his factory had made a mistake.

Case 2 - Telescopic Tube Patent Infringement

This case involves a vacuum cleaner telescopic tube **patent infringement**. This example of patent infringement involves an accessory for a vacuum cleaner.

Our company had continuously imported large quantities of a particular vacuum cleaner model from the greater Shanghai area. It had what is called a click-lock telescopic tube as one of the accessories. What we did not know was that a small German company (Carl Froh GmbH) had registered up to 20 different patents for the click-lock mechanism with European patent offices. Years had passed but this small company did not have the means to enforce their patent protection. Various Chinese manufacturers had copied part or all of Carl Froh's patents and were selling these click-lock telescopic tubes to many importers all over Europe.

A Finnish company (Rautaruukki Corporation) bought the majority shares of Carl Froh GmbH and eventually discovered that an asset they had acquired was Carl Froh's registered patents.

They did not take action immediately. Instead, they waited until the quantity of the imported click-lock telescopic tubes increased dramatically. Then they went into action by approaching all of the importers that had imported telescopic tubes for vacuum cleaners, thereby infringing on Carl Froh's patents. Compensation was demanded.

You can imagine that all over Europe millions of vacuum cleaners had been imported with these telescopic tubes and for Rautaruukki Corporation it was pay time.

We asked our patent lawyer for advice but he informed us that there was no way of winning the case in court even if we did want to go through the legal steps.

We and many other importers had to negotiate with the Finnish company. This meant financial compensation for each imported vacuum cleaner with the telescopic tube. The total amount we had to pay to the Finnish company exceeded US\$160,000 plus the cost of their and our lawyers.

The factory refused to repay any of the compensation payment. They told us that it was only an accessory that they had purchased from another company and that they were not liable for anything.

We employed an international law office in Shanghai and had several meetings with them. Our factory was in Suzhou, which is not too far from Shanghai. One of the lawyers even spoke fluent German making communications easier.

We provided them with all the evidence including copies of our P/Os clearly stating that we were **indemnified against any third party rights violations**. We also emphasized that considering the large amount of money involved, we were determined to proceed with a court case in China. Our lawyer helped convince the Chinese manufacturer to offer us an out of court settlement by refunding the requested amount.

The case was then settled amicably and we continued to purchase goods from that supplier.

Conclusion of the case:

1. The patent owner was right in his claim
2. We had not been negligent because nobody knew about the patents
3. The factory was only cooperative after we employed a local law office
4. Presenting our evidence did not convince them in the beginning
5. End consumers and customers were not affected because an agreement was reached
6. Since there was no comparable patent free replacement for the click-lock available, we could continue to import them but had to pay a royalty

Even after many years, your company can be sued for patent infringements because patent registrations cover long periods of time and you cannot escape your responsibility.

That means your supplier in China may no longer even exist or you are no longer doing business with him when a patent infringement is discovered.

If you want to have the slightest hope of recovering royalty fees paid in your home country, you must include indemnification clauses in all of your P/Os.

I am convinced that without the help of a local law office, we would not have succeeded in getting any money back. Through their arbitration, we averted a major disaster for our company. We were happy with the result because in the beginning we did not think any recovery could be achieved.

Case 3 – A Non-compliant Vacuum Cleaner

This case involves a vacuum cleaner **non-compliant with the EMC Law**. An electronic speed control caused a sales stop to be ordered by a local government authority.

We had sold more than 50K copies of a specific vacuum cleaner model with an electronic speed control feature to one of our German customers.

After some months the local government authorities (Bundesnetzagentur) approached our customer and informed them that they had tested several samples and found them to be non-compliant with the EMC laws (Electromagnetic Compatibility) because they exceeded specified emission limits. The electronic speed control feature was the culprit.

If it had been only one unit out of the five units tested, we could have argued that it was a single occurrence. Since all selected units showed the same problem, our customer was issued a complete sales stop for all EC countries.

At that time our customer still had approximately half of the imported quantity in stock and wanted to return approximately 25k vacuum cleaners to China.

This would have been a major disaster for us because their company policy requires that we refund the total amount before the vacuum cleaners are sent back to China for rework.

Sometimes, large powerful retailers do not want to accept reworked goods. In the event of a non-complying product, they have the law on their side when it comes to refusing reworked goods. They have also been known to first agree to the rework and later change their mind.

We had to find a fast solution that did not require returning the goods to China because that would require two ocean voyages plus the time for rework. The main point of the solution was to solve our customer's problem with the sales stop.

I after several negotiation sessions with the factory owner, he finally agreed to rework all remaining vacuum cleaners at our customers warehouse in Germany.

That might sound easy but unfortunately it is not. The factory had to send 11 workers including supervisors to Germany and they all needed passports and visas. Some of the workers had to travel to their hometowns to apply for their passport and we had to provide supporting documentation.

The factory had to obtain and ship acceptable replacement modules for the electronic speed control unit for every single unit.

To make a real long story short, it took the workers approximately 6 weeks to rework all of the vacuum cleaners at our customer's warehouse but they succeeded. Another lab test by the Bundesnetzagentur authorities confirmed the vacuum cleaners were now in compliance with the EMC regulation and the sales stop was lifted.

Total cost to the factory was approximately US\$60,000.00 plus travel and accommodation costs but considering the complete order value of more than US \$1,575,000 it was certainly the better solution.

Conclusion of that case:

1. The customer and the Bundesnetzagentur authority were right in their claim
2. We were not negligent because it is impossible to test every unit for EMC compliance during the Final Random Inspection that had been performed
3. The factory was not cooperative at the beginning
4. Presenting the evidence (breach of existing law in Germany) helped convince them
5. A solution was too time consuming because our customer had to wait several months before the case was settled. A return of the goods for rework would have been very costly, complicated, and the time required would have been longer
6. Our customer could continue with their sales as soon as rework progressed.

Our P/Os contained a clause that the factory must supply goods that comply with the existing laws at the destination country. The local government authorities proved with their own lab test report that the supplied units did not comply and were therefore not allowed to be sold in any EC country.

Our customer was forced to stop selling these goods in all of the 25 EC countries and had the option to return all unsold units to us or accept the rework.

Since the factory had agreed to our terms by signing our P/O, we had a stronger position to negotiate the rework deal with them.

For you as an importer, it is important to know that there are options to be considered other than only returning defective goods to your supplier, especially if the value is US\$1 million or more.

We were satisfied with the result because it helped to cover most of our expenses.

Case 4 – A Deep Fryer with Insufficient Cooking Temperature

A Deep Fryer with insufficient cooking temperature is an example of a **major quality issue**.

We had shipped larger quantities of a medium priced deep fryer under one of our customer's own brand names. The same model had previously been carried for several years in our product catalog. This is important for you to know because it was essential to the solution of this problem.

Our customer had an authorized lab test several units of the current production and the results were acceptable to their internal standards.

At a later time, our customer's QC reported high return rates caused by malfunction problems.

Our head office performed tests on the customer's return goods and found that the performance of the two thermostats was not according to specifications. The main thermostat was turning off the heat element before the selected cooking temperature was reached. In other words, you could not cook meat or French fries sufficiently.

I negotiated with the factory for the return and rework of approximately 22k deep fryers to China.

The manufacturer was in Ningbo and one of our engineers and myself visited the factory three times before an acceptable solution was negotiated.

The last meeting was attended by the usual 3-4 factory engineers, the sales manager, and the company owner. Mysteriously, an unknown and unIntroduced man also attended. We later learned the man was the factory's lawyer and advisor to the company owner for important decisions.

The arguments and the samples that we provided along with written documents and test results, finally convinced the company owner to accept the return of the goods for rework.

His problem was that he was seriously concerned that the Chinese authorities would take punitive action against his company due to the large number of returned goods. He also told us that his reputation would be seriously damaged because other factories would use this case to convince customers to buy from them.

That is also something you must consider when negotiating with Chinese suppliers. Try to find the real reason behind their refusal to replace or take back goods from their customers. It is not always only about money alone.

The deep fryers were sent back and the factory replaced the malfunctioning thermostats with new ones. The deep fryers now cooked properly.

You would think that settled the case and the reworked goods would be send back to our customer in Germany. Unfortunately, this did not

happen because as I mentioned in Case 2, retail organizations have the option of not accepting returned goods and can do this although they had agreed to accept the goods before.

That happened in this case when the head of the retail organization decided to drop their own brand of electrical products and they did not want to take the reworked goods back.

Since our company was doing a substantial amount of business with this customer and their market power is overwhelming, we had to accept their decision.

And because it was not the factories fault, we had to find another solution within our group of companies. The decision was to change the brand name and all of the packaging to our own brand name. Afterwards, the goods were finally returned back to our warehouse in Germany. The original retail organization then repurchased the rebranded and reworked deep fryers and put them back on their sales shelves.

Conclusion of the case:

1. The customer was right in their claim
2. We were not negligent because they passed the Final Random Inspection
3. The factory was not cooperative and it required three negotiation rounds to resolve
4. Presenting the evidence to them finally produced a successful negotiation
5. The customer was not cooperative when they did not follow through with the original agreement
6. Sales could continue after every single unit had been reworked and rebranded

The negotiations with that factory owner were very tough. I was threatened and yelled at but kept my calm and finally succeeded. I met the company owner several months later at the Guangzhou Fair and he hugged me. Obviously, my patience had paid off and even gained the respect of the factory owner.

In this case, it was very important to provide evidence that the large quantity of deep fryers really had a problem. I mentioned that we had been buying this model for some time and had our defect statistics that did not show any abnormal problems.

One typical factory owner's argument is that they are selling the model to many other customers around the world without any problems. That may even be true but it makes the negotiations even more difficult. You can imagine that when a factory owner secretly has a lawyer attending a meeting, anything could happen.

The factory obviously trusted their thermostat supplier from whom they were buying thermostats for many years. When incoming component inspection is not performed, defective goods can move undetected through the manufacturing and distribution processes all the way to the end user. That is what happened in this case. It should remind you not to take anything for granted.

In my other eBooks:

[How to Make Chinese Factory Visits More Successful](#)

- and -

[How to Assure Quality Imports From China](#)

I provide more detailed information about how factories must be evaluated and monitored to avoid their negligence from becoming your problem.

This claim was finally settled but the change of mind by our customer created extra problems for us and the factory because the rebranding took additional time and we had to keep the deep fryers in our warehouse for quite some time, which also cost us extra money.

Was that case solved? Yes, but not as we had expected and hoped and we were not satisfied with the result.

Case 5 – A Confiscated Stand Mixer

A stand mixer confiscated during an exhibit at a Trade Fair is an **example of a copyright violation**.

This case seems rather easy because it is only about a single unit but in reality, it caused us a lot of problems.

Several years ago we had a booth at the Domotechnica Trade Fair in Cologne. One of our exhibited models was a stand mixer that looked similar to a comparable model from Moulinex. The manufacturer, a large reputable Taiwanese company, had assured me that there was no copyright violation with Moulinex because they had investigated and did not find any problems.

On the second day of the fair, a lawyer employed by Moulinex and a bailiff from one of the Cologne courts came to our booth and confiscated our sample. They showed us a statement from the Moulinex designer confirming that our model violated his design because the resemblance was too great. Additionally they presented us with a court order enforcing Moulinex's request.

Because our company was registered in Hong Kong, the bailiff demanded a bond of DM 2,000 payable in cash within half hour otherwise our booth

would be closed down by him. We had also printed a photo of that model in one of our leaflets and we were required to black out the photo.

I immediately contacted our German patent lawyer and faxed him copies of the documents for his review. His immediate advice was to pay the bond and negotiate later. That is what I did.

The exhibition went on without further interruption for us but the case was not yet settled.

After returning to Hong Kong, I approached the German court for a refund of the bond but my efforts were in vain. Instead, they asked me to declare the number of stand mixers we had already sold and shipped to European countries, along with supporting evidence.

Fortunately, we had not sold or shipped a single unit. Because we only had the one sample from the factory, they finally gave up.

Conclusion of that case:

1. Moulinex was right with their claim
2. We were negligent by trusting our supplier's statement
3. The factory was cooperative and paid our expenses
4. The German court was not cooperative because they did not refund the bond

Don't rely on factory statements when they tell you they have already checked the product for copyright violations. Use your common sense instead. Look-a-likes that violate copyrights can be very expensive cases to resolve. We lost the DM 2,000.00 that was not refunded and we had lawyer fees. Had we shipped large quantities of that model to European

customers, we surely would have had to pay substantial compensation to Moulinex in one way or another.

This case was actually not about larger amounts of money or products but should open your eyes to what you can expect if you purposely import counterfeit products.

The supplier that claimed that the stand mixer did not violate Moulinex's copyright was requested to refund our expenses and he did to keep a business relationship with us. At least a little bit of a happy ending.

All of these incidents really happened. I hope they help you avoid similar problems for your import business. Considering how much time and money is involved to resolve them, it is a much better business strategy to put the effort into avoiding them all together.

Chapter 15 - How Much Time do You Need for Claim Settlement Negotiations?

As you can see from the previous examples, claim settlements usually cannot be reached overnight. From my experience, I would say that you have to talk to factory management (not always with the senior decision maker) at least 3 or 4 times before an agreement can be reached.

I mentioned before that the key decision maker is not always present during your negotiations. It is however essential that he be present during discussions of the final agreement. If not, you may have wasted your time and may have to look for other suppliers because this one obviously does not take your company seriously enough to be your business partner.

You made the necessary meeting arrangements in advance and have come a long way to see your supplier. If he does not willingly attend the settlement meeting and attempt to reach an agreement amicably, to a problem caused by his company, it is time to look for a new supplier.

That means you need to dedicate at least 3-4 days for negotiations to give your supplier some time to review your evidence and consider a fair solution.

The whole trip will take at least a week. When one additional meeting is needed to resolve your claim, you are better off staying another day and forgetting about the extra cost if it will get the claim resolved. When there is a larger amount of money being discussed, do not expect your factory will be easily convinced to churn out the money for you. Your negotiation preparations will perhaps prove decisive of the results.

Chapter 16 - Searching for New Suppliers if Necessary

If you realize that the negotiations are not going well and may not provide the desired results, you may want to take a break from them. During that break, you can look for new suppliers manufacturing the same or a similar product as the one you have filed a claim about.

Your other option, while taking a break from the negotiations, is to visit any other suppliers that you are familiar with in the area. Maybe one you have worked with before or one that you previously evaluated. It cannot hurt to see how their business is doing and if they have any new products of interest to you.

The latter one is of course much easier and more likely to succeed if you have a limited amount of time.

I always stress the importance of not putting all your eggs in one basket. That means you should try to find at least 2 or 3 other suppliers that potentially can replace the supplier you have a claim against in the event negotiations fail. If you return to the negotiations with this information, you will be more confident there are optional solutions and will have considerably strengthened your bargaining position.

Of course, if your supplier is the exclusive manufacturer of the product, you are in a much weaker position and the outcome may not favor you.

In chapter 23, I come back to this situation one more time.

Chapter 17 - Analyze Your Supplier's Compensation Proposals

After you successfully negotiate a compensation settlement, you need to step back and analyze any impact it will have on your business relationship with the supplier.

A Typical Supplier Proposal

Factories are usually very, very reluctant to provide any cash refunds to customers. For one thing, there are government controls in place that do not allow them to remit larger amounts of foreign currency to an overseas banking account.

Therefore, they will prefer to offer you a solution that does not involve cash. A typical proposal is to reduce the future sale price to your company for the product in question by a few cents per unit. Eventually you will receive the full value of your damages but you will have to buy a lot more product to receive it. This actually works to their advantage by keeping your company as a customer for a considerable time until the total amount has been "refunded".

They might offer to deduct US\$ 0.20 per unit from the current price of an electric toaster. If your claim compensation is US\$200,000, you will have to buy 1,000,000 toasters to recover your compensation. To your disadvantage, you will be bound to that supplier for a long time and have a diminished ability to react to changes in the marketplace. If another supplier enters the market with a more competitive product, you cannot react because you are committed. Your competition will grab the opportunity and take away sales back home.

On the positive side, if you do agree to this arrangement, your factory will survive and it will improve your long term relationship with the them.

Another Supplier Proposal

A similar but slightly different proposal is compensation in the form of FOC (Free of charge) goods. This is much more difficult for the factory because they have to purchase the materials and to produce the goods at not only their own cost but also their production capacity is lost while manufacturing the goods.

Also, under some conditions this solution is restricted by Chinese regulations that do not allow FOC shipments.

In the unlikely event that you do manage to obtain a large cash refund from the factory, you can expect price increases in near future as a way for the factory to try recouping their losses.

In some cases, the factory may offer you a combination of all of these solutions, some cash, some FOC shipments, and some price reductions.

You now know the impact these solutions will have on your business and can make the right decision.

Chapter 18 - Ask Home Country Authorities for Help

The local authorities in your home country may be willing and able to assist you in the claim with your factory. They have a very powerful tool at their disposal with the ability to blacklist suppliers that have seriously breached local regulations on a continuous basis.

If a factory has manufactured products that are a danger to the health of consumers or are even life threatening, EC authorities will prevent any further shipments from entering the EC territory until the case is resolved.

That is indeed a powerful tool because it will really would hurt your factory if a large order is involved. EC authorities can and will inform their Chinese counterparts. Once the two governments are involved, your supplier could be in dire straits.

Of course, this should be your recourse of last resort. It will permanently destroy the working relationship with your supplier and word of your action will likely pass to other Chinese factories. On the other hand, your business must survive and should not be made to suffer for mistakes made by your suppliers.

Chapter 19 - Can a Local Lawyer Help with Your Claim?

I definitely answer that question with a resounding “**yes**”. In case study 2 from chapter 14, you learned that we employed an international Shanghai law office for intermediate negotiations.

The lawyer we worked with even spoke German making communication with him much easier. He informed us about something that I did not know until that time, that the Chinese laws are not very different from our laws in Germany and that the Chinese Government used outside help when establishing their new legal system. What this amounts to, is legally everything is in place to prevent copyright infringement and other fraudulent business practices but...the enforcement is much more difficult than in Western societies.

Take, for instance, a product recall in the U.S. by an importer. The importer has to pay the cost of the recall. However, it remains next to impossible to take legal action in China to recover the costs and only in the rarest case can an importer successfully sue the supplier responsible for a product failure. Since most suppliers are paid in full, well before the goods arrive at the destination port, the importer does not enjoy the leverage that comes with owing payment to the supplier.

Chinese courts have no obligation to enforce judgments rendered in the U.S. or European courts and thus, a contractual provision calling for U.S. or European litigation is a mistake if the Chinese party does not have sufficient fixed assets within the United States or Europe to satisfy the judgment.

On the other hand, Chinese courts are generally obligated to enforce foreign arbitral awards, and to attach assets in satisfaction of such awards, pursuant to China's treaty obligations. As a result, it is far easier to collect on an arbitral award in China than it is to collect on a foreign court judgment in China.

With that said, care should be taken in drafting an international arbitration clause with a Chinese entity. China has special rules that must be followed in order to ensure the enforcement of an arbitral provision or arbitral award in China; in this regard, importers of Chinese goods should consult with an IDR lawyer (Informal Dispute Resolution) for specific advice on the drafting of a Chinese arbitration clause.

Hiring a local lawyer with knowledge of the international laws involved, can therefore certainly help you either to proceed with lawsuits or to avoid them through arbitration. The latter is more desirable because it will help you to save time and most likely money. Having an interpreter for your most important negotiations is fine but having professional legal advice may make the most difference.

International lawyers in Hong Kong or Shanghai are not cheap. You should inquire with them regarding their fee and add that cost onto the total amount you are trying to recover before you make a decision here. For smaller cases, it may not be worth it to get a lawyer involved at all.

The magic word is here "Arbitration". Finding a solution outside of the courts is better for all parties. You may also underestimate how much information is exchanged between Chinese suppliers. They are usually busy people but do get together for fun and relaxation. They will not hesitate to tell other factories that they have been unjustly treated, whether it is fully true or not.

Having said that, I suggest that for high value claims you employ a local lawyer. At least to the extent that they advise you how to proceed next.

Chapter 20 - Sealing an Agreement with a Handshake is Not Enough

It should be common sense that after your long and hopefully successful claim negotiations with your supplier, any agreement arrived at must be documented in writing.

A handshake would certainly not be enough to finalize your agreement. Everything that has been agreed to by both parties has to be documented in great detail in a contract signed by the appropriate managers of both companies.

Factories may hire lawyers to review these contracts and my advice is for you to do the same unless you have studied law and are familiar all the legal aspects of contract law.

It is essential and I speak from experience with these types of cases. Leave nothing to doubt about your agreement and also no room for multiple interpretations of what has been agree to.

Chapter 21 - Ask Your Factory for a Corrective Action Plan to Prevent the Recurrence of a Similar Claim

After everything is agreed upon and the contract is signed by both parties, there remains one important point that has to be finalized before you go home. Having reached an amicable settlement with your supplier is good for your business but you must make sure that your factory takes the right actions to avoid similar problems in future.

If your home country authorities discovered a regulation violation, they will certainly want to make sure that the events are not repeated. They may even require proof that it will not be repeated before you can resume importing. This is usually accomplished by supplying them with a corrective action plan from your supplier.

What Exactly is a Corrective Action Plan?

This is an expression that you hear quite often from certification organizations when a product is found to be out of compliance with existing directives or regulations.

Non-compliance with an existing directive or regulation can give your company a big headache if your supplier does not have the competence or willingness to take corrective actions.

The factory has to prepare a technical document explaining in great detail what changes will be implemented immediately. It must apply to all new production in order to assure full future compliance with the existing regulations and directives. The document must be supported by photos, technical drawings, or any other information necessary to assure full compliance.

If it is a technical product the factory must apply for new certificates and may have to change the model number as well.

I suggest you consider a new model if it is your own brand because your customers may be very reluctant to continue buying the same model after the authorities called for a nationwide sales stop. It is always good to inform them that you have changed the model number because major improvements have been implemented.

Chapter 22 - Talk to Your Inspection Company's Management

If your inspection company overlooked the reason for the claim during their Final Random Inspection, you must talk to their management and negotiate for compensation. Since your inspection company is usually not involved in any sales activities and is not located in mainland China, it is easier to obtain a cash refund from them if you can prove their liability.

Inspection companies are also insured for cases of this type and considering the large numbers of inspections they perform for customers, mistakes can happen. If mistakes happen too often, you should consider replacing them with a different inspection company to prevent imperfect products from being shipped.

At the same time, you have to ask yourself whether you provided sufficient information to your inspection company to complete the work properly. If they did not receive clear instructions or samples, the fault may be on your own and they will take this position if you approach them for compensation.

If your company did nothing wrong, you should also discuss with your inspection company what actions they will take to avoid similar problems in future. It is in their self-interest to avoid claims because it would damage their reputation along with the financial losses.

I should also mention that sometimes factories successfully bribe inspectors to prepare a "Passed" inspection report for them. A nice dinner, some gifts, or some cash may help to convince the inspector to do them that favor.

Therefore, it is not uncommon for large inspection companies to investigate the performance of their inspectors on a regular basis and replace any “black sheep” as soon as they become aware they are not performing their duties in an acceptable manner.

Do not take me wrong and begin thinking of your inspection company as your enemy because they are actually your best ally in preventing major factory claims in China.

Chapter 23 - Do Not Waste Your Time with a Disagreeable Supplier, Start Talking with a New Supplier Instead

After you have three or more meetings with your supplier's decision maker without getting any results, it is time to make your own decision.

Suppliers know that it will cost you time and money to replace them and they speculate that you will not do it. **Give them a surprise and move on to another supplier.**

You now understand why it is always good to have several suppliers for the same products in your back pocket. If you have backup suppliers, begin talking with them immediately after you become aware that a claim will be filed with your current supplier and long before your business trip to negotiate a settlement.

Since rumors spread very fast in China, your other supplier(s) may have already learned about your problem and can come up with a fast solution for you. However, do not make the mistake of taking for granted everything that your potential new supplier is telling you. You must apply the same due diligence and maybe much tougher requirements towards the new supplier as you did with the current supplier to be sure you do not have the same problem again. Unless the supplier has been evaluated recently, a full evaluation will need to be done.

During this process, you might be surprised to learn that your new supplier can offer you a better price and better service than your existing supplier does. In the end, you may even benefit from the claim against the first factory.

Moving on to a new supplier does not mean that no action will be taken against your existing supplier. However, it should be obvious that your ability to obtain compensation or replacement of the goods will be much more difficult once your existing supplier has learned that he has been left behind.

The full satisfaction of your customers at home must be your first priority. If that is best achieved by replacing your disagreeable and uncooperative supplier, you have already solved the greatest part of your problem.

Chapter 24 - Epilog

I am confident that my eBook will help you to **Settle Factory Claims In China More Successfully** and perhaps can help you to avoid them altogether. After all, claims with Chinese factories are not inevitable when your company takes the right precautions on a continuous basis.

Potential factory claims are at times predictable if you monitor the production quality coming from your factories closely. Your newly established QC department (I hope that you have listened to my advice) will assist you and alert you when trouble is looming around the corner.

If you have monitored 4 factories over a certain period and one of them falls short of your expectations frequently, get rid of it and you will have fewer future problems.

During the research for my seven eBooks I came to realize that most resources available to new importers primarily focuses on the easier portions of the import business. What importers really need is experience based advice about preventing claims against factories in China and if they do occurred, how to solve them.

I would like to express my gratitude to you for buying this eBook from me and hope that you will also consider some or all of my other eBooks as well.

Klaus-Dieter Hanke