Step-in right: safeguarding critical supply relationships in contracts

The step-in right (right of entry) gives a contracting party the right, in certain crisis situations, to step directly into the position of a supplier or subcontractor, or to take over their performance or assets. In industrial procurement it serves as a tool for supply assurance, for example in cases of insolvency, refusal to perform or failure of critical suppliers. The term originates from project and plant construction and from PPP contracts, but has gained considerably in importance in supply contracts and framework agreements. For buyers, it is a central element of an effective risk mitigation plan for critical materials.

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Key facts at a glance

01 The step-in right allows direct entry into the contract level of a supplier or subcontractor upon defined triggers such as insolvency or performance disruption.

02 Typical triggers are insolvency petitions, refusal to deliver, quality defects with stockpile risk or breaches of compliance obligations.

03 What matters most in practice is the cooperation obligation: the step-in only works if intermediate suppliers and sub-tiers are contractually obliged to consent.

04 Exercise is often tied to deadlines, termination logic and procurement approval thresholds; legal details should be examined on a case-by-case basis.

05 In the context of the Supply Chain Due Diligence Act and rising supply chain risks, the step-in right is gaining weight as a second safeguarding instrument alongside risk diversification.

06 Without clearly documented process roles in accordance with procurement roles (RACI), the right often remains theoretical in a crisis.

Definition: step-in right

The step-in right is a contractual arrangement that grants an entitled party – typically the buyer or end customer – the right, upon the occurrence of defined events, to enter into existing contract or

performance levels. It is intended to secure the continuity of critical supplies and services where the immediate contracting party fails or materially breaches its obligations. Legally, it is generally a contractual entitlement; actual enforceability depends heavily on the contract structure and the cooperation of further contract levels.

Distinction from other safeguarding instruments

Unlike a right of withdrawal or a contractual penalty, the step-in right is not directed against the direct contracting party but at taking over or continuing a performance at lower levels. It complements classic instruments such as second-source strategies, safety stock and vendor managed inventory (VMI), but does not replace them. While risk diversification reduces the probability of failures, the step-in right primarily addresses the impact of a failure that has already occurred.

Use cases in industrial procurement

In practice, the step-in right is frequently found in plant construction, in long-running framework agreements, in single-source relationships and for components with long lead times. In consortia, the question of step-in can also become relevant if a consortium member fails. Further applications are licence agreements in which manufacturing rights are to pass to the buyer in the event of disruption, as well as logistics services in the context of 4PL models.

Methods and approach for contractual implementation

A functional step-in right does not arise from a single clause but from a coordinated contract architecture across several levels. Central is the back-to-back obligation: the main contractor must oblige its own suppliers to consent to the end buyer's direct step-in in the event of disruption. Without this chain, the right remains imperfect.

Defining triggers (step-in events)

Triggers that are as objectively verifiable as possible increase legal certainty. Commonly cited are the opening or filing of insolvency proceedings, persistent payment arrears, refusal to perform, repeated delivery delays above defined thresholds, substantial quality defects and serious compliance breaches. Threshold values should be harmonised with the material class classification and the criticality of the component.

Anchoring cooperation and information obligations

The direct contracting party should be obliged to report trigger events immediately, disclose subcontracting chains and cooperate in the transfer in the event of disruption. This includes transfer declarations, information rights regarding order and production status, and the right to continue using production equipment, tools or test documentation to the defined extent. Confidentiality and intellectual property must be expressly regulated in this context.

Establishing price and transition logic

In practice, it has proven worthwhile to define in advance the conditions under which the step-in takes place – such as the continued validity of existing prices, compensation for work commenced and the treatment of advance payments. Without such provisions, a negotiating compulsion arises in a crisis from a position of weakness. Procurement approval thresholds should define who may order a step-in and may bear the budgetary consequences.

Important KPIs and review criteria for step-in arrangements

The effectiveness of step-in agreements can be measured where procurement organisations systematically monitor the safeguarding of their critical supply relationships. The focus is on coverage rate, currency and exercisable residual capability of the contractual chain.

KPIs at a glance

Typical benchmarks from practice: the share of critical materials with an effectively agreed step-in or transfer protection should generally be well above two thirds. The documentation rate – i.e. evidence that the cooperation chain extends to the relevant sub-tier – should typically exceed 90 %. The response time from trigger event to step-in decision should frequently remain below five working days.

Integration into existing reporting systems

Step-in KPIs belong on the agenda of regular supplier reviews, in addition to lead time, quality and delivery performance metrics. Within S&OE, trigger indicators such as payment irregularities or capacity bottlenecks can be monitored continuously and linked to contractual early warning levels.

Risks and controls in dealing with step-in rights

The greatest risk is the false sense of security: an agreed step-in right that is not legally or practically enforceable in an emergency offers no protection. Likewise, unprepared exercise can trigger compliance, quality and intellectual property risks.

Legal and tax review

The enforceability of step-in agreements – particularly in insolvency and across multiple contract levels – is complex and depends on the specific design and the applicable legal system. Tax consequences of a transfer, for example in the case of making facilities or licences available for use, are also case-specific. These questions should be reviewed by legal and tax advisers before the contract is concluded; this article does not constitute legal advice.

Operational controls and preparation

Effective control means: incorporating step-in scenarios into the bow-tie analysis of critical supply paths, keeping transition documentation (drawings, test equipment, residual capacities) maintained and ready, and anchoring the exercise in the series approval process and procurement approval thresholds.

In addition, a risk mitigation plan should describe who decides in the event of disruption, which alternative sources are activated and how communication with the supplier takes place.

Compliance and supply chain

In a step-in, the buyer effectively assumes responsibility along the supply chain. Requirements under the Supply Chain Due Diligence Act, product safety such as RoHS, and sustainability obligations up to Scope 3 emissions and SBTi target reporting remain applicable during the transition period and must be integrated into the due diligence concepts.

Current developments and digital implementation

Rising supply chain disruptions, geopolitical uncertainties and tightened compliance requirements mean that step-in clauses are being negotiated more frequently and earlier. At the same time, technical possibilities are growing to digitally map the transparency of sub-tiers and production status required for this.

Supply chain transparency as a prerequisite

A step-in presupposes knowledge of the supply chain. The procurement data model and supplier master data are therefore increasingly extended with sub-tier information, manufacturing locations and licence rights. Digital exchange formats such as cXML support the system-assisted maintenance and reconciliation of this master data via supplier portals.

Strengthened position of foreign and smaller suppliers

As part of resilience programmes and the debate on critical materials, buyers are increasingly demanding transfer rights even from small single-source suppliers. Suppliers respond with price premiums for such securities; buyers should weigh the value of the step-in right against alternatives such as dual sourcing, stockholding or in-house manufacturing rights.

Interaction with financing instruments

Supply chain finance also affects the step-in question: instruments such as reverse factoring can stabilise the liquidity of key suppliers and thus prevent trigger events from arising in the first place. Step-in rights and financial safeguards are therefore complementary elements of an overall concept for supply assurance.

Typical metrics

Metric	Typical value
Coverage rate of critical materials with step-in protection	> 70 % *typical benchmark for critical material classes with a single-source share*

Documentation rate of the cooperation chain	> 90 % *share of contracts with demonstrable back-to-back pass-down to the relevant sub-tier*
Response time from trigger to step-in decision	< 5 working days *common practical target with documented responsibilities in accordance with RACI*
Review cycle for step-in clauses	12 months *frequently chosen interval for reviewing triggers, prices and contact lists*

Practical example

A medium-sized mechanical engineering company sources a critical cast component from a single-source supplier who, in turn, depends on a core manufacturer as a sub-tier. After a peer in the industry had to wait months for a replacement part, the buyer revises the contract architecture. Objective: in the event of disruption, production at the sub-supplier should be able to continue directly without the intermediary.

- Anchoring a back-to-back clause in the main contract with an obligation to pass the step-in consent right down to the foundry sub-supplier.
- Definition of objective triggers: insolvency petition, two consecutive on-time delivery breaches, or a quality hold stock above a defined threshold.
- Storage of the contract references and transition documents in the procurement data model; assignment of the decision-making role in accordance with procurement roles (RACI) to the category manager.
- Supplementary inclusion of the scenario in the bow-tie analysis and the risk mitigation plan for the material class "critical cast components".

Conclusion

The step-in right is a powerful but demanding instrument for safeguarding critical supply relationships. Its value stands and falls with the contract architecture: without cooperation chains down to the relevant sub-tier, without clear triggers and without a prepared transition logic, it remains paper. Buyers should understand it as a building block alongside risk diversification, safety stocks and financial safeguards, and regularly review its effectiveness using KPIs. Legal and tax details belong on the agenda of qualified advice in every concrete project. Those who do this homework significantly shorten the recovery time in a crisis.

Frequently asked questions

? What does step-in right mean in simple terms?

The step-in right is a contractual right of entry: it allows a buyer, in defined disruption scenarios, to step directly into the position of a supplier or sub-supplier and continue the performance. Its purpose is to secure critical supplies, for example in cases of insolvency or refusal to perform. Enforceability depends heavily on whether all contract levels are obliged to cooperate.

? When does a step-in right apply?

Typical triggers include the supplier's insolvency or insolvency petition, substantial payment arrears, refusal to perform, repeated delivery delays or serious quality and compliance breaches. The events should be defined as objectively as possible in the contract, with thresholds. In individual cases, the legal effectiveness of the trigger cascade must be assessed separately.

? Is a step-in right enforceable in the event of insolvency?

This is the most critical question of the instrument: insolvency law provisions may restrict its exercise, particularly where contracts or rights are already affected by the administration of the estate. Careful design – such as separate transfer agreements with sub-tiers – improves the prospects. Whether a specific clause will hold up in insolvency should always be reviewed legally on a case-by-case basis.

? How does the step-in right relate to the Supply Chain Due Diligence Act?

Anyone exercising a step-in effectively assumes control over an affected value-added stage, and with it the associated duties of care and verification. Requirements under the Supply Chain Due Diligence Act, product standards such as RoHS and sustainability reporting remain relevant during the transition period. The step-in process should therefore be integrated into the existing due diligence organisation.

? What does a step-in right cost for suppliers?

Suppliers frequently demand a risk premium on the price or compensation regarding intellectual property and manufacturing rights for such securities. In practice, typical premiums are in the low single-digit percentage range of the affected volume, depending on criticality and negotiating position. The effort should be weighed against alternatives such as second sourcing or safety stock.

? How do you implement a step-in right contractually?

As a minimum, the following are required: defined triggers, information and cooperation obligations of the direct supplier, a back-to-back clause for passing the step-in right down to sub-tiers, and provisions on prices, transition and intellectual property. In addition, internal preparation with documented responsibilities and transition documentation is recommended. Legal and tax review form part of the implementation process.

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