

Robinson+Cole

Recent Trends in Contract Negotiation and Business-to- Business Dispute Resolution

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Please Note

This roundtable is designed to provide accurate information about the subject matter. However, it only provides general information and does not constitute legal advice. No attorney-client relationship has been created. If legal advice or other assistance is required, let us know directly.

Preliminary Considerations

- This platform should not be used for activities prohibited by antitrust law.
- Avoid discussions leading to a restriction, or coordination, of competition between or among attendees.
- Attendees should not share information, have discussions, and/or make arrangements on, among other things, pricing, market conduct, terms of sale, individual manufacturing costs and costs of sale, output, or supplier or customer relations/allocation.

Why are we here?

- Evaluation of risk in contracting remains critical for manufacturers of all sizes
 - Supply Chain Shift: Playbooks & Templates
 - Focus More On Risk Than Size Of Contracts
 - Renewed Focus on Vendor Contracts
- Leverage Remains Paramount
 - Presentation will focus on both sides
 - LTA and non-LTA situations
- Trends in B2B Dispute Resolution Flow Back To Contract Negotiation (and Vice-Versa)

The Anatomy of a Contract

- **Business Terms**
 - Term
 - Pricing
 - Change Orders
 - Volume
- **“Legal Terms”**
 - Change of Control
 - Indemnification
 - Liquidated Damages
 - Intellectual Property / Confidentiality
 - Regulatory Compliance
 - Warranties
 - Force Majeure
- **Beyond the Checklist: Areas of Renewed Focus**

Trend #1: Change of Control

28.3 Assignment

Seller shall not assign any of its rights or interest in this Agreement or any Order, or subcontract all or substantially all of its performance of this Agreement or any Order, without ██████████ prior written consent. Seller shall not delegate any of its duties or obligations under this contract. Seller may assign its right to monies due or to become due. No assignment, delegation or subcontracting by Seller, with or without ██████████ consent, shall relieve Seller of any of its obligations under this Agreement or prejudice any rights of ██████████ against Seller whether arising before or after the date of any assignment. This article does not limit Seller's ability to purchase standard commercial supplies or raw material.

The prohibition set forth in this GTA Section 28.3 includes, without limitation (and the following shall be deemed to be "assignments"): (i) a consolidation or merger of Seller; (ii) a change in the ownership or voting rights of more than fifty percent (50%) of the issued and outstanding stock of any corporate Seller; (iii) any assignment or transfer which would otherwise occur by operation of law, merger, consolidation, reorganization, transfer or other significant change in corporate or proprietary structure; (iv) the sale, assignment or transfer of all or substantially all of the assets of Seller; and (v) where Seller is a partnership, a change in control in such partnership.

Change of Control (cont.)

- Issue Spotting:
 - “Without prior consent” / No Reasonableness Language
 - No language – “which shall not be unreasonably withheld”
 - Absence of reasonableness standard
 - Split of authority
 - 14 states: Withhold consent unreasonably
 - 18 states: Read into contract
 - Assume Reasonableness Is In Contract
 - Party prohibited from withholding consent to obtain economic concessions. See *R.B. Robbins v. Hunts Food & Industries, Inc.*, 64 Wn.2d 289 (1964).
 - But: Can withhold consent if economically prejudiced or harm. *Washington Wine & Bev. Co. v. Outlook Vineyards*, 1999 Wash. App. LEXIS 2058, at *19 (Wash. Ct. App. 1999).

Change of Control (cont.)

- Trend: No Consent Needed for Corporate Reorganization / Restructuring
 - Particularly as PE becomes more involved with supply chain

"Notwithstanding the foregoing, Supplier may assign the Order and the Contractual Documents in their entirety without consent of the Purchaser in connection with a corporate reorganization."

Trend #2: Indemnification

• Typical Questions

Excerpt from Robinson+Cole Model Playbook

- Indemnification:** If we have indemnification obligations, are they limited to our negligence or willful misconduct? Yes: No: N/A:
- (a) Do we have an obligation to defend? Yes: No: N/A:
- (b) Do we have an obligation to indemnify for direct claims (i.e. claims that an indemnified party has against us)? Yes: No: N/A:
- (c) Is the other party required to indemnify us for their negligent or willful misconduct? Yes: No: N/A:
- (d) Is the other party required to indemnify us if a product is defective due to their design, specifications or material they contributed? Yes: No: N/A:

Indemnification (cont.)

9. INDEMNIFICATION; FEES AND EXPENSES:

Tenant shall pay, and *shall protect, defend, indemnify and hold the Indemnified Parties harmless* from and against all *liabilities, losses, damages, costs, expenses (including attorneys fees and expenses), claims, demands or judgments* of any nature arising or alleged to arise from or in connection with the following events any claim or liability in respect of any adverse environmental impact or effect, whether such environmental conditions existed, developed or were created prior to or during the term of this Lease . . . provided, however, that the foregoing indemnity with respect to any Indemnified Party shall not extend to any such liabilities, losses, damages, costs, expenses (including attorneys fees and expenses), claims, demands or judgments [that] result from the willful misconduct of such Indemnified Party.

Landlord shall give prompt written notice to Tenant of any and all such claims and suits. Tenant, at its sole election, may defend by counsel selected by Tenant, and approved by Landlord and Mortgagee, which approvals shall not be unreasonably withheld or delayed, any and all suits which may be brought, and claims which may be made against the Indemnified Parties, or in which the Indemnified Parties may be impleaded, upon any such liability, loss, damage, cost, expense, claim, demand or judgment.

Indemnification (cont.)

- Use of Indemnification Provisions in Intra-Party Disputes Becoming More Prevalent (Search for Attorneys Fees)
 - Even though there are notice provisions, selection of counsel and payment not due until the party becomes obligated to pay
 - The language above resulted in litigation that lasted 6 years
 - Summary judgment on this issue was denied
- Courts are Split on this issue
 - Compare *Hooper Associates, Ltd. v. AGS Computers, Inc.*, 74 N.Y.2d 487 (1989) ("the court should not infer a party's intention to waive the benefit of the rule [that parties are responsible for their own attorney's fees] unless the intention to do so is unmistakably clear from the language of the promise")
 - With *Battelle Memorial Institute v. Nowsco Pipeline Services., Inc.*, 56 F. Supp. 2d 944, 951 (S.D. Ohio 1999) ("it is clear from both the Ohio and Sixth Circuit definitions of indemnification that a party wishing to narrow an indemnification clause to third party damage is obligated to limit the scope of the clause expressly; and absent such express limitation, indemnification clauses may apply to damage suffered by the contracting parties themselves").

Indemnification (cont.)

- Mitigate the Risk:
 - Include a specific exclusion for intra-party disputes: “*This provision does not apply to intra-party disputes between the parties.*”
 - If you wish to add it, expect resistance.
 - Put a monetary cap on your aggregate liability for intra-party dispute damages.
 - Narrow the indemnification “nexus phrase” (i.e., what events will trigger intra-party indemnification).
 - “*...losses solely resulting from [the indemnifiable event]*” vs. “*...all losses arising out of or related to [the indemnifiable event]*”

Trend #3: Liquidated Damages

- Trending
 - Supply Chain: Internal Policies Prohibiting All Forms
 - Use of Caps
 - Caps Not Sufficiently Defined/Limited
 - Failure to State Sole and Exclusive Remedy
- Trying to Limit Exposure
 - Limit to Specific Breaches
 - Limit When a Claim Can be Made

Liquidated Damages (cont.)

- Penalty vs. Liquidated Damages
 - Courts Take One of Two Approaches – Enforceability
 - Classic Approach: Looks at the reasonableness of the liquidated damages amount as of the time the parties entered into the contract. If the amount was a reasonable estimate at the time of contract formation, it will be enforced, regardless of the actual damages.
 - Consider Whether Construed As Penalty or For Liquidated Damages (use of “liquidated damages” generally not enough)
 - Two considerations:
 - If amount stipulated is conscionable
 - Based on nature of transaction, actual damages not easily and readily determinable
 - Modern Approach: Determines the reasonableness of the liquidated damages provision, taking into consideration the actual damages.
 - A term fixing unreasonably large liquidated damages is void as a penalty.

Trend #4: Cost-Savings Provisions

- A. Cost Reductions. The following provisions apply to the Parties' efforts to reduce the costs of LTA Parts:
1. SUPPLIER and BUYER agree to use good faith efforts to identify and implement cost reductions in SUPPLIER's cost of LTA Parts. Such efforts may include a) appointing of capable personnel by SUPPLIER and BUYER to a cost reduction team, b) cooperating together in identifying potential cost reduction ideas, c) using good faith efforts to implement cost reduction ideas that are recommended for implementation by the cost reduction team, d) reporting as reasonably requested by BUYER the status of cost reductions and e) participating in cost reduction programs established by BUYER.
 2. Except as otherwise agreed in writing, all reductions in SUPPLIER's cost of LTA Parts which arise **out of the joint efforts** described above will be appropriately shared between the Parties hereto, and SUPPLIER shall reduce the unit cost of LTA Parts to accordingly. .
 3. Cost reductions on LTA parts resulting from changes in Buyer's specifications shall exclusively be passed on to Buyer in the form of cost reductions in the unit prices of LTA parts.
 4. SUPPLIER shall promptly report to BUYER all cost savings realized through the cost reduction team effort that affect any LTA Parts.

Cost-Savings Provisions (cont.)

- Starting to see more attention to these provisions throughout the supply chain (particularly in aerospace)
- Cost Savings Programs: Impact Margins
- Buyer Side: Make sure language is comprehensive (“joint efforts”)
- Seller Side: Make sure language gives you room to develop process changes that improve margins

Trend #5: Most Favored Customer Provisions

Most Favored Customer. Seller shall not at any time sell the same Goods to a different buyer at prices below those stated in this Agreement. If Seller charges a different buyer a lower price for these Goods [under similar quantity and delivery conditions], Seller must immediately apply the lower price for the Goods under this [Agreement/Order]. If Seller fails to meet the lower price, Buyer, at its option, may terminate this Order without liability pursuant to this [Agreement/Order's termination provision].

Most Favored Customer Provisions (cont.)

- Becoming increasingly common, especially in supplier agreements
- Seller Circumvention/Mitigation Techniques:
 - Limit to similarly situated customers
 - Limit to a certain transaction, product and/or time period
- Intra-Party Enforcement Issues
- Antitrust Issues
 - Rule of Reason
 - Market power of the parties involved
 - Business purpose of the agreement
 - Competition in the relevant market

Trend #6: Force Majeure

- Trending: Supply Chain Slowdowns or Shortages

Force Majeure. Seller shall not be liable or responsible to Buyer, nor be deemed to have defaulted under or breached this Agreement, for any failure or delay in fulfilling or performing any term of this Agreement, if such failure or delay is caused by or results from acts beyond Seller's control, including: (a) acts of nature; (b) flood, fire, earthquake or explosion; (c) war, invasion, hostilities (whether war is declared or not), terrorist threats or acts, riot or other civil unrest; (d) requirements of Law; (e) actions, embargoes or blockades in effect on or after the date of this Agreement; (f) action by any Governmental Authority (whether or not having the effect of Law); (g) national or regional emergency; (h) strikes, labor stoppages or slowdowns or other industrial disturbances; (i) shortages of or delays in receiving raw materials; or (j) shortage of adequate power or transportation facilities (each, a "Force Majeure Event").

Force Majeure (cont.)

- Force Majeure Declaration Issues/Considerations
 - Triggering Event
 - Mitigation Efforts
 - Customer Allocation
 - Set-Off
- Increased Costs as Excuse for Non-Performance?
 - Absent an explicit contractual provision, seller must demonstrate either the “essential nature of the performance” was altered or there is a “severe shortage of raw materials or of suppliers”
 - “Sole Source Defense” – Parties must *explicitly* contemplate that performance of the contract relies on the performance of a single supplier and there is a failure from that one supply source.

Force Majeure (cont.)

- Seller Side:

- Cover a wide range of events that give rise to excused performance
- Limit the buyer's express contractual remedies when performance is excused

- Buyer Side:

- Draft the provision as narrowly as possible
- Limit the definition of force majeure events
- Include the ability to terminate the contract if a force majeure event continues for a specified period of time

Trend #7: Regulatory/Conflict Minerals

- Focus on conflict minerals originating from the DRC region and adjoining countries.
- Population: 75 million
- Since 1998: 5.4 million people died
- Congress: Regulations last decade
- Purpose: Prevent companies from engaging in trade that supports regional conflicts ~ reduce funding



2017 Recent Developments

- Trump administration considering suspending the regulations for 2 years
 - Draft executive order leaked in February 2017
 - No executive order has yet been signed
- SEC has suspended enforcement of provision requiring that companies label their products as “DRC Conflict Free”
 - Follows lengthy litigation over the legality of this aspect of the regulations
 - SEC is reviewing the regulations in light of the litigation
 - Other requirements in regulations remain in effect

Companies Impacted

- **Publicly traded companies**
 - Who file reports with the SEC under the Exchange Act.
 - Who voluntarily file reports with the SEC under the Exchange Act.
 - Applies to domestic and foreign companies.

- **Privately held companies**
 - As a supplier in a publicly traded company's supply chain.
 - Compliance under U.S. sanction law
 - SEC rulemaking comments: Although does not apply to private companies, expect that “commercial pressure” will lead to companies voluntarily providing conflict minerals disclosures

International Conflict Mineral Regulation

- European Union
 - Status: On March 16, 2017, the EU Parliament adopted EU conflict minerals regulations.
 - Regulations to take effect January 1, 2021
 - Applicability:
 - Rule would apply to “high risk” and “conflict-affected” areas (to be defined later by group of experts)
 - Mandatory due diligence required for companies involved in the smelting or import of the minerals.
 - Smaller companies trading in minerals would be exempt.
 - **Voluntary disclosure for companies** whose products contain conflict minerals.

Other Contractual Provisions

- Trending
 - Overlook Boilerplate Language
 - Governing Law & Jurisdiction Clauses
 - Conflicts of Laws
 - United Nations Convention
 - Forum Selection Clauses
 - State-by-state variation (mandatory or permissive)
 - Non-Competition Clauses
 - Vendor Contracts
 - Arbitration

Dispute Resolution Considerations/Ethics

- Letters of Intent/Memoranda of Understanding
 - Enforceability
 - Can be a good template for key deal points, both in the beginning and at the end.
 - Disclaimer is critical: *Notwithstanding anything to the contrary herein, this letter of intent is not intended to be binding upon the parties. Any commitment will necessitate the negotiation and execution by both parties of a mutually satisfactory “XXXXX.”*
- Clarity v. Ambiguity
 - Purposeful ambiguity
 - “Meeting of the minds” doctrine is largely obsolete.
 - Fraud in the inducement is not.

Conclusion

Questions?

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THE APPLICATION OF THE ATTORNEY-CLIENT PRIVILEGE OUTSIDE THE UNITED STATES

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