



Contract Building Blocks

Puts the Law on your side
Keeping the process legal

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April 14, 2009

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Presentation Outline

- Uniform Commercial Code
- Contract Law
- Top 25 Check-List for a Contract
- Contract Pitfalls
- Q&A

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Uniform Commercial Code

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Uniform Commercial Code

- Article 2 Sales
- Article 3 Commercial Paper
- Article 4 Bank Deposits and Collections
- Article 5 Letters of Credit
- Article 6 Bulk Transfers

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Uniform Commercial Code

- Applies mostly to Goods not Services
- Contract Law vs. UCC
 - Your contract should supersede UCC
 - Where your contract is weak or does not apply the UCC steps in.
 - UCC tends to favor the Buyer
 - Not all States are the same

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Contract Law

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Bodies of Law

- Statutes - Codes
 - Federal
 - State
 - Local
 - UCC – Each State is different
- Common Law
 - Contract derived from old English Common Law
 - Judges Opinions and Precedence
 - UCC was coded around Common Law

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Basic Definitions

- Goods
 - Office Supplies
 - Steel
 - Motors
- Services
 - Engineering
 - HVAC
 - Facilities
 - May have deliverables
- Information
 - Technology
 - Hardware

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Types of Sourcing Agreements

- Purchase Orders
 - Battles of the forms - Acknowledgments
- Confidentiality Agreements
 - Stand Alone Agreement
 - Paragraph in Agreement
- Master Supply Agreements (MSA)
 - Items to negotiate
 - Items you don't change
 - Divide into goods, services & Information

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Enforceable Contract

- Reality of assent
 - Meeting of the minds
- Agreement
 - Offer and Acceptance
- Consideration
 - Quid pro quo – Something for Nothing
- Contractual Capacity
 - 18 or older
 - Authority
- Legality
 - Contract that provides a legal service or product
 - Not against public policy
- Form
 - Whatever form the law requires
 - Value over \$500 and Real Estate must be in writing

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Express vs. Implied Contracts

- Expressed
 - Explicitly stated
 - Agree to buy a friend's iPod for \$50
 - Signed apartment lease
- Implied
 - Actions or your conduct
 - Paint the wrong house

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Buyer vs. Seller Contracts

- If you have to take the Seller Contract, what to look for.
- What the Buyer contract should consist of.
- Issues that you think are taken for granted and burn you down the line.

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Top 25 Check List for Contracts

Jurisdiction	Venues	Dispute Options	Amendment	Tooling
Considerations	Definitions	Term & Termination	Quantity	Quality
Packaging	Specification - SOW	Payment	Price	Notice
Title - Ownership	Delivery	Attachments	Signature	Force Majure
Warranties	Remedies	Damages	Indemnity & Insurance	Limitation of Liability

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Jurisdiction

- The local laws that will apply to the contract
 - State of Delaware
- Must be stated in the contract

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Venues

- Location of court for papers to be filed.
 - Cost to file
- Must be stated in contract.

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Dispute Options

- Court
 - Seller may want you to waive a jury trial
- Alternative Dispute Resolution – ADR
 - Negotiations
 - Mediation – Third Party
 - Arbitration – Third Party
 - Binding vs. Non-Binding
 - American Arbitration Association
- When to use it
 - Sole or single source
 - David vs. Goliath
 - Doctrine of unclean hands

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Amendment

- Agree on how changes will be made
- Services – Change Orders
- Mail, Express, Fax, Attention
- In writing

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Tooling

- Who owns the tooling
- Who owns the design for the tooling
- Who maintains the tools and how
- Who will pay to move it
- Bailment – Right to come in and take the tooling without court order

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Consideration

- Make sure you have a section on consideration
- “The parties, as in good and Valuable consideration”
- 1:3 parts that make up a contract

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Definition Section

- Use this section to define and clarify the definitions of specific words throughout the contract
- Helps a judge in a dispute over definitions
- Examples:
 - Equipment – Gas Compressor and Spare Parts
 - Software – Design and Code

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Term & Termination

- Renew Automatically – Evergreen Clause
 - Advise against this, too hard to track.
 - May be locked in for 90 days to a year.
- Renew Upon Agreement
- Renew at Option on One Side
- Expires on a set date
- Survive Contract Termination
 - Liability
 - Confidentiality

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Quantity

- Must state quantity
- One shipment or split shipments
- Installments, state quantities and dates
- Seller has the right to ship the complete contract

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Quality

- State quality assurance requirements
 - What must be tested
- Buyer inspection has no time limit
- Seller Defects
 - Credit
 - Rebate
 - Replacement
- State Return Authorization Process

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Packaging

- Packing Specifications
 - Crating
 - Waterproofing
 - Industry Standards
 - Ocean vs. Land Requirements
- Who pays for it
- Container Markings
- Documentation

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Specification – Statement of Work

- Buyer required specifications
 - Mostly off the shelf
 - Sensor parameters
- Statement of Work (SOW)
 - Something off the shelf
 - Deliverables
 - Milestones
 - Right of Inspection
 - Acceptance Criteria
- Should be an attachment

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Payment

- Procedure of paying invoices
- Payment Terms 30/60/90
- Matching Material to Invoices
- Funds, Check, Credit Card & Wire
- A/P Contact Information
- Right to off set or reduce payment

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Price

- Firm
- De-Escalation Clause -1,3, and 5 year contract with built in price reductions, based on efficiencies
- Escalation Clause – Based on an Index (CPI), or an agreed upon increase.
- Details of cost breakdown
 - Materials
 - Labor
 - Currency
 - Overhead
 - Profit

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Notice

- Method of Notice
 - Certified mail, return receipt request
 - Express mail
 - Hand deliver
- Attention
 - Copy attorney and/or Buyer
 - Specific address

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Title - Ownership

- Intellectual Property – Work for hire
 - Patents
 - Trademarks
 - Copyrights
 - Trade Secrets
- Indemnification for use of patentable product. (Indemnification)
- Warranty – Free and clear title

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Delivery

- INCO TERMS (International Commerce terms)
 - FOB
 - FAS
- Risk of Loss – ROL
 - FOB Seller or Buyer Dock
 - Required Insurance
 - Take Pictures
- Spell it out

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Attachments

- Incorporate seller literature
- Pre contract seller communication regarding product
 - Seller promises
- Specifications
- Statement of Work – SOW
- Original RFQ

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Signature

- Ensure who has signing authority
- Assume agency authority
- Have the seller sign first
 - Three Copies
- Cover letter and track transmittals

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Force Majure

- View this as Excusable Delays
- Act of God
 - Flood, Rain, Snow
- Do not Accept
 - Seller employee strike (UPS)
 - Material delay from subcontractors

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Warranties

- Warranties of Goods
 - Title – free and clear
 - Free from defects
 - Complies with specifications
- Warranties for Services
 - Acceptance
 - Comply with scope of work

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Warranties

- Implied Warranty
 - Warranty of Fitness for Merchantability
 - Should work for its intended use (Hammer, Software)
- Expressed Warranty
 - Warranty of fitness for particular purpose
 - Spelled out in contract
 - Specific to the specifications or SOW
 - Seller will want to remove this

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Warranties

- Mean Time Between Repairs (Data)
- When does the warranty start
 - Supplier ship date
 - Buyer receipt date
 - Customer receipt date
- How long is the warranty
- Does the supplier have the service infrastructure to handle warranty repairs

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Remedies for Breach of Contract

- Basic Remedies
 - Repair
 - Replace
 - Return
- Additional Remedies
 - Right to resell
 - Cover – Reimburse for difference in cost
 - Injunction – Stop Work
- Must state in contract

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Damages

- Actual/Direct – Actual documented costs
- Consequential/Indirect – Lost Profits
- Incidental – Legal Fees
- Liquidated – Agreed to by both parties
- Seller will want Limited Liability
- Evaluate your risk
 - Network down for two hours, \$1 Million in sales
- Must state in contract

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Indemnity & Insurance

- Seller will want Buyer to indemnify Seller for all claims and legal costs
 - Remove Any and All Negligence.
 - Change to Sole Negligence
 - Second round accept proportionate.
- Evaluate your seller's insurance requirements.
 - Auto, Workers Comp & General Liability
 - Certificate of Insurance
 - Named as additional insured
 - Cancellation Notice

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Limitation of Liability

- Seller will want to have no or limited liability.
- Limit financial responsibilities
- Evaluate what your total exposure would be
 - Loss of sales
 - Rework
 - Switch Supplier Costs

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Benjamin Franklin

"By failing to prepare, you are preparing to fail."

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Pre Contract Work

- Supplier vs. Buyer Contract Terms
- RFQ Two Parts
 - Scope or SOW
 - Contract Terms and Conditions
- Project Time Lines – Last Minute Negotiations
- Negotiation Matrix – Example next Slide
- Beyond the handshake

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Negotiation Matrix

XXX VENDOR							
Issue	Weight of Concern	Supplier Offer	Buyer Offer	Accepted Offer	Score	Weighted Score	Notes
Price / Cost	3	\$948,000.00	\$879,452.00	\$911,452.00	2	6	
Payment Terms	1	Net 30	2% 10, Net 30	2% 10, Net 30	3	3	
Lead-Time / Delivery	2	6 Weeks	4 Weeks	4 Weeks	3	6	
Inventory in Days	3	30 Days	60 Days	45 Days	2	6	
Warranty	2	12 Months	36 Months	24 Months	2	4	
Liquidated Damages	2	\$50,000	\$100,000	\$50,000	1	2	
Contract Length	3	3 Years	2 Years	2 Years	3	9	
Freight	2	FOB Supplier	FOB Buyer	FOB Buyer	3	6	
Risk Of Loss	2	Supplier Dock	Buyer Dock	Buyer Dock	3	6	
Volume Commitment	2	500,000	300,000	300,000	3	6	Documented 80% of Sales
SLA Reports	3	Quarterly	Monthly	Monthly	3	9	
Quality Reports /Cert.	2	Monthly	With Shipment	With Shipment	3	6	
Include One Year Spare Parts	1	No	Yes	No	0	0	
Software Copy Rights	1	No	Yes	Yes	3	3	
Software Escrow	1	No	Yes	Yes	3	3	
Software Upgrades	1	No	Yes	Yes	3	3	
Escalation / Reduction Clause	1	3%	CPI	CPI	3	3	
Total Possible Score	96						
Total Score						81	
Percent of Possible Total						84%	

Contract Phases

- Pre-Contract
 - RFQ-Detailed Specifications - SOW
 - Negotiations – Level (1,2 & 3)
- Contract Execution
- Post Contract
 - Administration and Tracking
 - Breach
 - Notice of Material or Minor Breach

Domestic vs. International

- Domestic Contracts
 - UCC – Uniform Commercial Code
 - Statutes
 - Common Law

- International
 - CISG – Convention on Contracts for International Sales of Goods Administration and Tracking
 - World Court – United Nations Charter

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Business Ethics

A reporter once asked a Fortune 500 CEO about ethics. He said “I would not want to do anything that my Mother would be embarrassed about reading in the paper”

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Business Ethics

- Win / Win vs. Win/Lose Relationship
- Look at some of the Fortune 500 companies.
- Toyota Production System (TPS)
- Win/Lose will lose in the long run

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Win-Win Negotiation

- ***Characteristics of win-lose negotiation--***
 - Rigid negotiating positions
 - Argument over a fixed amount of value
 - Strict use of power by one party over another
 - Adversarial competition played out at the negotiating table

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Win-Win Negotiation

□ **Characteristics of win-win negotiation--**

- Parties try and understand each other's needs and wants
- Parties build on common ground and work together to develop creative solutions that provide **additional** value
- Primary use of power is to focus on common rather than personal interests
- Likely to engage in open sharing of information

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Win-Win Negotiation

□ **Win-win negotiation applies only to certain situations—**

- Strategically important items or services
- Trust between parties exists
- Both parties endorse a win-win approach

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Negotiation Conclusions

- **Successful purchasing negotiators share some common attributes--**
 - They realize that training, planning, and practice are required to become an effective negotiator
 - They have higher negotiating goals and aspirations than their counterparts
 - They are destined to be among an organization's most valued professionals

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Purchasing Ethics

- Ethics: the set of moral principles or values guiding our behavior.
- Three rules of ethics buyers must follow:
 - A buyer must be loyal to the organization
 - Must act ethically towards suppliers
 - Must uphold ethical standards of the profession

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Risks of Unethical Behavior

- ❑ Legal risk – Legal penalties could ensue as a result of unethical behavior.
- ❑ Personal risk - Buyer's professional reputation could be at risk.
- ❑ Company risk – Company's reputation could be at risk.

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Supporting Ethical Behavior

- ❑ Developing a Statement of Ethics
- ❑ Top Management Commitment
- ❑ Closer Buyer-Seller Relationship
- ❑ Ethical Training

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Supporting Ethical Behavior

- ❑ Developing Consistent Behavior
- ❑ Internal Reporting of Unethical Behavior
- ❑ Preventive Measures

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ISM Reference websites

- ❑ Bid Specifications Database
<http://www.ism.ws/tools/BidSpec/index.cfm?navItemNumber=13232>
- ❑ Ethical SCM
<http://www.ism.ws/membership/content.cfm?ItemNumber=4740&navItemNumber=13237>
- ❑ eTool Agreements <http://www.ism.ws/products/results.cfm?MetaDataID=487&navItemNumber=13185>

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Questions

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