Establishing a Successful Outsourced Manufacturing Relationship

An Interactive Look at the Business Models and Industry Norms Underlying Successful EMS Contract Negotiations

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To successfully negotiate with a Contract Manufacturer ("CM"), one must understand the CM industry, the CM business model and the CM’s concerns.

The decision to contract with a CM is a business decision driven by the Customer’s Procurement or Manufacturing Operations who understand the CM role.

Customer’s lawyer [whether in-house or outside counsel] is often involved after the decision to engage the CM has been made and often after pricing and other significant “deal” terms have been agreed upon.
Customer’s lawyer is often “educated” by the Customer’s Operations people on the relationship “specifics” during the contract negotiations and in front of the CM.

Often, Customer’s lawyer is only asked for input on the basic Ts & Cs (maybe even just the “legal” terms if there is an in-house procurement contracts group) and not the implementation exhibits (i.e., the operational/business/financial requirements).
Overview of the Contract Manufacturing (CM) or Electronic Manufacturing Services (EMS) industry

The CM business model and how it drives contract negotiations

Examples of typical customer contract provisions and CM contract provisions. Why the CM takes a particular stance

Examples of negotiated clauses… where the parties tend to meet
Understanding the Terms

Contract Manufacturer ("CM") or Electronic Manufacturing Services Provider ("EMS")
- Provides manufacturing and supply chain services

Electronic manufacturing services (EMS)
- Since 1989, the "EMS" term has been generally replaced by the term "Contract Manufacturer" or "CM" but EMS is still a term that most companies recognize as applying to the contract manufacturing services business
  - EMS is a term used for companies that provide design, testing, manufacturing and return/repair services for electronic components and assemblies for customers

Customer
- The party that contracts with the CM to have products manufactured

Original Equipment Manufacturer ("OEM")
- A product design owner and manufacturer which sells products to other entities, that are sold under the buyer's trademarks/branding (e.g., think Emerson TVs sold by Sears under the Sears brand, so end user purchasers look to Sears for warranty/other services)
Today the Contract Manufacturing services industry is a global industry with total revenues in excess of $275B and providers operating in more than 60 countries.

The industry is generally considered to have 4 tiers of competitors, based upon revenue:

<table>
<thead>
<tr>
<th>Revenue Tier</th>
<th>Est. Companies</th>
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<tbody>
<tr>
<td>Tier I: Rev. &gt; $3B</td>
<td>8</td>
</tr>
<tr>
<td>Tier 2: Rev. $.5B to $3B</td>
<td>26</td>
</tr>
<tr>
<td>Tier 3: Rev. $.1B to $.5B</td>
<td>68</td>
</tr>
<tr>
<td>Tier 4: Rev. less than $100M</td>
<td>11,800</td>
</tr>
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CMs are also generally divided into three functional sectors:

- Low – Mid Volume and Highly Complex Products
- Mid – High Volume and Mid Complexity Products
- High Volume and Simple or Low Complexity Products
History of the CM Industry

For at least 75 years, companies have been using third parties to manufacture/bring their products to market

First, companies contracted with parties with a product to exploit in their market, and these companies were willing to buy the product from an OEM that would attach the company’s brand and generally accept back-to-back responsibilities to the product that the companies would accept related to the product for which the company had to accept liability due to the relationship

SCI (then Space Craft Inc.; now Sanmina-SCI) is generally credited for being the first major EMS /contract assembly company in North America
By 1999, there were more than 3,000 CMs in the world serving a rapidly growing $58B market.

The top 5 companies all had sales in excess of $2B and accounted for about 40% of the industry’s market share.

CMs now offer a wide range of services in addition to manufacturing services:
- Material procurement
- Material planning
- Supply chain options
- Supply chain management
- Multi-site manufacturing options
- Engineering Services
- ODM Services
What is a CM? What is it Not?

CMs
- Are manufacturing “services” providers
- Manufacture Customer’s “unique” or custom Products
- Manufacture Products to Customer’s specifications
- Purchase materials at the direction of Customer
- Can offer economies of scale by providing manufacturing services for many customers at facilities in low-cost locations

CMs
- Are not suppliers, per se, of Products – they provide “services”
- Do not “own” the product: Products are built at the direction of the Customer
- Do not engineer Products or instigate design changes
  - Unless those services are specifically negotiated in a separate provision or contract totally unrelated to the original request for manufacturing services (i.e., a design services transaction)
What do CM’s do for Customers

Material Procurement
- Based on Customer forecasts, order material to meet anticipated Product demand and any demand flexibility requirements

Supply Chain Management
- Negotiating prices and warranties with material Suppliers. Managing the relationship between Customer and Supplier

Provide cost efficient manufacturing options
- Location options, skilled workforce
The Customer- CM Relationship

Customer owns the Product IP and Product design
- CM makes engineering changes at Customer’s direction

Customer hires CM to manufacture the product as an extension of Customer’s own manufacturing line
- CM owns its own manufacturing processes

Customer makes all marketing/commercial exploitation decisions concerning their Products
- CM may assist with physical distribution/logistics, but has no input on other marketing/commercial exploitation of Products

Customer is responsible for Product design, IP, improvements, service, etc.
- CM is responsible for manufacturing in accordance with Customer’s specifications
The Customer and CM Responsibilities

- Customer determines market requirements
- CM should drive the planning and scheduling of the factory and lower level materials
- CM should drive process improvement and cost reduction
- CM shares resources across other customers doing similar activities
- Incentive to be efficient in CM – Manufacturing is a profit center
The Customer- CM Risk/Reward Profiles

Customer Responsibilities
without CM Partnership
• R & D
• Intellectual Property
• Product Marketing
• Distribution
• Customer Service
• Supply Chain Management
• Logistics
• Manufacturing
• New and Continuing Product Research

CM Partner Responsibilities
• Supply Chain Management
• Manufacturing
• Logistics

Customer Business Model
Risk/Reward Profile
• Product Innovation Risk
• Product Development Risk
• Market Risk
• Execution Risk

Targeted gross margins: 45% to 70%

CM Business Model Risk/Reward Profile
• No Product Innovation Risk
• No Product Development Risk
• No Market Risk
• Execution Risk

Targeted gross margins: 6% to 10%
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<tr>
<th>Global</th>
<th>Euro-Centric</th>
<th>Asia-Centric</th>
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<tr>
<td>• Foxconn</td>
<td>• Elcoteq</td>
<td>• Kinpo</td>
</tr>
<tr>
<td>• Plexus</td>
<td>• Zollner</td>
<td>• Venture</td>
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<tr>
<td>• Flextronics</td>
<td>• Enics</td>
<td>• Beyonics</td>
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<tr>
<td>• Jabil</td>
<td>• Videoton</td>
<td>• Alco</td>
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<tr>
<td>• Celestica</td>
<td>• Partner Tech</td>
<td>• Nam Tai</td>
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The CM Industry Top 12 Companies- Market Shares

2007 EMS Market Share

- Foxconn: 16%
- Flextronics: 12%
- Jabil: 5%
- Celestica: 3%
- Sanmina-SCI: 2%
- Elcoteq: 2%
- Kinpo Group: 1%
- Venture: 1%
- Benchmark: 1%
- Plexus: 1.0%
- Siix: 0.7%
- Asteel: 0.6%
- Asteel: 0.3%
The average Manufacturing Services Agreement (MSA) with a CM

- Has a duration of approximately 1.8 years before being re-negotiated
- Covers services valued at approximately $11M

Larger contracts can sometimes cover 5 years and represent in excess of $1B

Approximately 1 out of every 15 users of CM services does so without any contract in place

1 in 9 contracts inadequately define key issues such as material liability, IP ownership, etc.
Overview of CM Contract Considerations

Risk vs. Reward is the largest motivator

Traditionally, the CM business is based on low risk and a low profit margin

As the CM industry has matured – and Customers have become increasingly “decoupled” from the manufacturing process – many users of CM services have attempted to shift uncompensated risk onto the CM Provider. Risks do not disappear.

The shifting of risk from one company to the other is the DOMINANT ISSUE in most CM contract negotiations. An inordinate amount of emphasis is placed on issues that have a lower than average risk of a problem.
CM contracts (MSAs – manufacturing services agreements) are financial documents with legal footnotes; financial and risk considerations are the drivers for the CM.

Negotiations between Customer and a CM are driven 90% by Operations and not the lawyer. Otherwise, Legal costs rise as issues are argued which are not relevant to the relationship, pointing out all possible outcomes, etc.

Customer’s attorneys usually provide an OEM oriented agreement. Even after the “education process” on the Customer-CM relationship, the original OEM document is used as a basis for the CM relationship. This requires substantial change and drives up cost, time, and frustration.
## Contract Terms: Customer v. CM Perspectives

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| Nature of Agreement| • Customer sees agreement as a Purchase and Sale Agreement (or a Supply Agreement), where Customer is purchasing a finished product and thus has traditional expectations that a seller should be responsible for and absorb risks of selling product.  
• Customer sees CM as “Seller” and Customer as “Buyer” with traditional UCC notions of risk. | • It’s a manufacturing “services” contract and CM is “services provider”, where CM provides manufacturing services to build Customer’s product for Customer (making the Product per Customer’s requirements).  
• The specifications, requirements, designation of components and vendors (at least in the beginning of the relationship) are all the responsibility of Customer.  
• CM has no control over design or engineering of the Product or the specified components or even the process and certainly not the marketing or selling.  
• CM is driven by what the Customer tells CM. |
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<td>Some CMs may also take on designing and engineering services – usually another agreement (design services agt.): CM still limits its responsibility and liability, because CM is still performing these services using Customer’s requirements. The margins the CM makes on design services may be a little higher than contract manufacturing (10%-15%), but are nowhere near the Customer’s margins (40%+) to commercially exploit the product (i.e., marketing margins, etc.).</td>
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| Risks, generally   | Customer wants to shift risks to CM without (or with little) compensation  
  ○ Even if Customer understands that it held risks before the decision to outsource, the idea of shifting costs and risks to CM is part of their thinking: it’s “CM’s skin in the game”  
  ○ Customer’s Legal views the products manufactured by the CM from a standpoint of an “end-user” (Legal provisions which protect the end-user to the max) | CM can’t take risk without compensation because margins are already so low; if Customer wants CM obligation greater than CM’s standard position, then Customer needs to pay for this risk shift |
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| Warranty (reactive remedy) | • Products will meet/conform to/comply with specifications  
  • Customers want long warranty periods (12-18-24 +) months  
  • Warranty on spares the longer of 180 days or the remaining warranty period of the product into which the replacement spare is installed | • Products will be manufactured in accordance with specifications; i.e., “workmanship” (CMs can’t absorb liability if the Customer’s specifications are incorrect)  
  • Warranty period of 90 days is sufficient to flush out manufacturing defects; otherwise, longer warranty periods add extra cost that Customer must bear  
  • Warranty on spares is the shorter of 90 days or the remaining warranty period of the product into which the replacement spare is installed |
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<td>Environmental Warranties (i.e., RoHS, WEEE)</td>
<td>• Products will comply with RoHS/WEE/other environmental laws &lt;br&gt; • Customer wants CM to be liable for environmental warranties on components that CM uses (not just manufacturing processes, solder paste/solvents, etc. used in manufacturing processes) &lt;br&gt; • Customer wants CM to warrant environmental law compliance even if Customer won’t agree to change materials in order to achieve compliance</td>
<td>• CM generally will warrant that its manufacturing processes (and materials CM controls to use in manufacturing process, like solder paste/solvents, etc.) are environmentally compliant &lt;br&gt; • CM will generally warrant components that it owns (examples: antennas, camera modules, power supplies used in cell phones) – as CM is the materials manufacturer and IP owner in these situations. Margins are greater in these situations.</td>
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| Epidemic Failure (proactive remedy) | - CM should be responsible for component epidemic failure as well as epidemic failures due to poor workmanship  
- Wants epidemic failure remedy available for the life of the product  
- Wants unlimited liability for CM  
- Customer wants CM to assist with all epidemic failure activities at no extra charge | - CM is willing to discuss some limited epidemic failure remedy based upon bad workmanship/manufacturing (i.e., a prospective remedy for a breach of the workmanship warranty, since normal warranty breach remedy is a reactive remedy)  
  - Epidemic failure related to manufacturing defects only lasts as long as the agreed-warranty period (if a longer period, then this will have a cost);  
  - CM wants a financial cap on CM liability (per event or overall cap) for manufacturing defects that become epidemic failures; |
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<td>Epidemic failure of components:</td>
<td>CM takes the same position as warranty regarding components – this is the vendor’s responsibility, and CM will pass through any vendor warranty if CM has the contract or otherwise facilitate Customer/vendor resolution if CM is managing the AVL of Customer.</td>
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<td>For epidemic failures not due to CM’s fault, CM will assist Customer in resolving problem but required activities of CM need to be specific and Customer must pay CM for its assistance costs</td>
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<tr>
<td><strong>Components</strong></td>
<td>Customer wants CM to be liable for component defects (i.e., warranty that components will meet their specifications)</td>
<td>Component vendor warranties are passed through to the extent vendors permit this; otherwise, CM will facilitate interaction w/ vendors to get Customers satisfaction but will not be liable</td>
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| **Supply Chain**   | • Customer is willing to provide forecast (nonbinding) and wants maximum flexibility (without cost) in cancellation, rescheduling if its forecasts and customer demand are not accurate  
• Customer wants CM to hold materials without cost | • CM’s ability to know when to purchase components (and how much), and ability to predict and deal with spikes in demand, whether safety stock is needed, capacity upside is dependent upon Customer demand, forecasts, historical data, so Customer mistakes are not a liability of CM  
• If Customer wants a demand-pull (kanban) hubbing arrangement instead of standard forecast, PO, invoice fulfillment process, then specific requirements apply instead of standard provisions |
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<td><strong>Supply Chain (con’t)</strong></td>
<td>- Customer wants CM to use best efforts to use materials with other customers or in CM’s own processes or to return them to the vendor without (or with little) liability to Customer</td>
<td>- CM is generally willing to absorb some risk/liability based solely on CM-caused mistakes (i.e., ordering mistakes) but not those of the materials vendors</td>
</tr>
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</table>
| **Materials Management** | - Customer continues to want to manage the vendors, and Customer generally has its own approved vendors (AVL), often contracts in place with good terms/pricing, etc.  
- Customer wants the CM to be liable for noncompliance of the vendors with the materials contracts in place, including breaches of warranties, epidemic failures, IP indemnification, late deliveries | - CM would like to take more control over the materials vendors supply chain and to move Customer to CM’s current vendors for nonunique materials in order to take advantage of lower pricing that CM can get for volume purchases over a number of customers (PPV benefit to CM) |
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<tr>
<td>Materials Management (con't)</td>
<td></td>
<td>- if Customer wants to retain its vendors and has contracts in place with good pricing/terms, then CM should be permitted to purchase under the Customer/vendor contracts</td>
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<td></td>
<td></td>
<td>- CM cannot absorb vendor liability but will facilitate warranty returns and liability discussions between Customer and vendors and CM can often use its strong relationship with vendors to get a more beneficial resolution for the Customer (but no guarantees and no liability of CM if unsuccessful)</td>
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| Obsolete Materials | Customer wants determination of obsolete materials to be a long period (i.e., 180 days +), with CM holding materials without charge | • CM wants determination that materials are obsolete as soon as an engineering change (or some other factor) causes materials to no longer work for the product (generally less than 60-90 days); holding obsolete parts has a cost that CM does not want liability for  
• CM will allow longer periods for determination of obsolescence if Customer pays for holding charges |
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| Excess Materials   | - Customers want to define Excess Materials in terms of “nonuse for a longer period of time, in case Customer might be able to provide a more accurate forecast in the future that requires use of the Materials or there’s an unforecasted spike in demand or Customer might have unreasonable “upside capability” expectations based upon its sales group’s assurance of demand  
- Customer wants CM to hold excess, without regard to CM’s capacity constraints, all without additional costs  
- Customer wants to require CM to use “best efforts” to use the Excess Materials in CM’s own processes or those of other customers, regardless of whether these Excess Materials are “popcorn” (nonunique) or unique to Customer needs | - CM cannot take on financial liability for Customer’s mistakes in forecasting vs. actual orders, EC changes caused by Customer fault (design, new customer requirements, etc. );  
- CM may have sufficient power in the “popcorn” group of components that it can provide Customer with some supply chain control and force-back of liability to the component vendor (especially if CM has component vendor contract privity and numerous customers for whom CM buys popcorn parts) |
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<tr>
<td><strong>IP Ownership</strong></td>
<td>• Customer owns all IP related to its Product</td>
<td>• CM owns all IP related to its manufacturing processes (and, if CM owns any components, then CM owns IP related to components as well)</td>
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<tr>
<td><strong>IP Licenses and IP Indemnification</strong></td>
<td>• Customer wants a royalty-free license to CM’s IP for its manufacturing processes to use during relationship and to take and use on its own or with other CMs (including competitor); • Customer believes that CM should take on risk of IP indemnification because of CM’s participation in the manufacturing process</td>
<td>• CM’s position is that, while they may have “manufacturing and testing processes” that might be subject to IP protection, the CM’s primary benefits to an Customer are based upon its business acumen, supply chain relationships and cost models and efficiencies/accuracy in manufacturing the Customer’s products rather than the CM’s manufacturing process IP; • CM is willing to grant Customer a license to CM’s manufacturing process IP during the relationship and may agree to allow Customer to continue to use the CM’s manufacturing process IP if Customer decides to take the manufacturing back in-house, but generally won’t allow Customer to continue this license after</td>
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<td>(particularly if CM has any vertically integrated supply chain elements, like an ODM), and CM should absorb liability for supply chain vendor component IP infringements</td>
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<td>the MSA term to allow the Customer’s next CM to use the current CM’s IP</td>
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<td>• Customer doesn’t believe it should indemnify CM against any Customer IP infringement claims</td>
<td></td>
<td>• CM can’t absorb the potential liability of an IP infringement related to the product due to (i) components in the Customer Product; or (ii) any element of the Customer’s product other than the CM’s manufacturing process that infringes the Customer’s or any Component Supplier’s IP or to software/design or any other element that might infringe another party’s IP or otherwise cause personal injury/death. Customer has the marketing margins to cover potential IP infringement, where CM’s margins are minimal and cannot cover this risk (see bullet after next below)</td>
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<tr>
<td>• Customer grants a license to CM of its Customer IP needed</td>
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<td>• CM will pass through to Customer any IP infringement indemnification obligations that the Component Supplier grants to the CM (to the extent</td>
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<td>Contract Provision</td>
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<tr>
<td>to manufacture the product Customer wants CM to manufacture, but often wants to extract higher levels of security obligations on the CM, depending upon where the CM is manufacturing the product, including separate manufacturing lines, other customers of CM have no access to areas where CM is manufacturing Customer’s products; certificates regarding CM employees attesting to personal liability in the event the employees leave the CM with knowledge of the Customer’s IP. As an example, if the CM is manufacturing in China, the Customer might demand that the CM compensate their employees who will be involved in the Customer’s product manufacture with sufficient amounts to ensure the employee’s loyalty, noncompete (if the employee leaves for another CM) and/or bonus or that pass-through is possible), and CM will “facilitate” the follow-through of the relationship between the Customer and the specific component vendor (to the extent that CM has taken over the supply chain responsibility, but if Customer has retained this relationship, CM is limited in its ability to assist Customer with the component vendor’s obligations to the Customer</td>
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- As to CM’s position on IP indemnification: CM’s margins are between 2-5%, CM doesn’t have an extensive IP legal group to vet and pay for investigation into potential competitor IP rights nor
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<td>other compensation/retention programs to dissuade the employee from the potential of taking the Customer’s IP and disclosing it to others</td>
<td></td>
<td>the IP knowledge as to Customer’s IPR; moreover, the Customer has upwards of 30%-50% margins on the sale of its products in a reseller distribution system and up to 85% margins on end user sales; in addition, the Customer has its own IP legal group (either in-house or outside counsel) and is free to use its product research allocations and potential sales margin to pay for potential IP infringement issues</td>
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<td></td>
<td></td>
<td>• Additionally, it is the Customer that determines where it wants to market the products around the world and can make an informed decision as to whether to pay for the proper IP infringement review/assessment as to potential in-country potential infringements related to the Customer’s IP</td>
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<td></td>
<td>• Often the CM is a “deeper pocket” than the Customer and a third party will look to sue anyone in the chain of manufacture – CM needs Customer protection against infringement claims re Customer IP</td>
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| Other Indemnification | • Customer wants CM to indemnify for a CM breach or noncompliance with any provision of the MSA, in addition to traditional personal injury/death and also property damage  
• Customer doesn’t believe it needs to provide CM with any indemnification | • CM will indemnify for personal injury/death as a result of defective workmanship (warranty breach)  
• CM may also indemnify for tangible property damage (with a cap) as a result of defective workmanship (warranty breach)  
• CM may indemnify for breach of warranty re: materials CM elects to use in manufacturing process (solder paste, etc.) |
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<td>Limitation of Liability</td>
<td>• Customer wants CM to be liable for all consequential damages associated with a breach by CM of its warranties, a breach of or noncompliance with any provision of the agreement or a delay in providing services (including OTD delivery of products)</td>
<td>• CM doesn’t have the profit margins to accept these consequential damages nor can CM control the extent of the remedies the Customer may offer to their customers. One claim could potentially erase all profit from the entire relationship and severely damage the CM</td>
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<td></td>
<td>• Customer wants unlimited financial cap on direct damages</td>
<td>• CM’s low profit margins on manufacturing services can be wiped out with one claim if there is no financial cap on damages of all kinds (except death/personal injury due to CM’s failure to manufacture in accordance with specifications—workmanship defects caused by CM)</td>
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<td>On-Time Delivery and Penalties</td>
<td>• Customer wants CM liable for delivery delays, caused by manufacturing</td>
<td>• CM can’t be financially responsible for delivery delays of supply</td>
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<td>issues or purchasing materials solely within CM’s control but ALSO</td>
<td>chain vendors and needs to keep schedule flexible to provide Customer</td>
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<td>caused by supply chain vendors</td>
<td>with updated lead-times on an on-going basis</td>
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<td>• Customer usually wants some financial penalty related to failure</td>
<td>• CM may be willing to accept some heightened responsibilities for</td>
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<td>(a high percentage of “OTD” = e.g., 95%+), often from Day 1 of the</td>
<td>“popcorn” material vendor delivery commitments when CM has broad</td>
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<td></td>
<td>relationship, even if the Customer was not receiving this OTD from</td>
<td>needs for this popcorn across wide number of customers and so</td>
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<td></td>
<td>its own supply chain vendors when Customer had captive manufacturing</td>
<td>normally carries inventory with some flexibility of moving</td>
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<td></td>
<td>in-house</td>
<td>inventory among its Customers, particularly when Customer</td>
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<td></td>
<td></td>
<td>forecasts are not always accurate</td>
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<td></td>
<td></td>
<td>• CM more willing to accept some limited delay penalties for reasons</td>
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<td></td>
<td>solely within the CM’s control (i.e., manufacturing process issues,</td>
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<td></td>
<td>CM mistakes in ordering materials, CM-owned materials</td>
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<td></td>
<td></td>
<td>o penalty amounts must be very limited because CM margins are</td>
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<td>already so low</td>
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# Contract Terms: Customer v. CM Perspectives

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| Tooling            | Customer wants CM to buy/house tooling specific to Customer, with right to purchase tooling from CM at end of relationship at fully depreciated value | CM prefers Customer to pay for or immediately reimburse CM for tooling costs (and to pay overhead costs in space used for tooling)  
• CM may be willing to invest in cost of Customer tooling if the manufacturing transaction is large enough, but wants price of tooling to be allocated over a projected volume of products, with a balloon payment after a certain period of time if the actual volumes are less than the projected volumes |
## Contract Terms: Customer v. CM Perspectives

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<tbody>
<tr>
<td>Prototypes</td>
<td>Customer wants a substantial number of prototype units for free, and wants all warranties to apply to these units</td>
<td>CM understands that prototypes are generally much more expensive to build than production units, because the production volume efficiencies do not apply in one-off prototypes. Prototypes generally cost 5x+ what production units cost. Further, because they are preproduction units, there is no guarantee that these prototypes will meet any warranties normally associated with production units, either from the CM warranties of “manufacturing in accordance with specifications” or the Customer’s warranties that it provides to its customers. These units are “AS IS” because they are test units, created for both parties in the relationship to analyze and fix to be able to proceed to the production units</td>
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## Contract Terms: Customer v. CM Perspectives

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| DFM                | Customer wants a substantial number of DFM units for free, and wants all warranties to apply to these units | • DFM units are by their nature early, pre-manufacturing level units so they aren’t meant to be available for commercial sale so they don’t include warranties  
• DFM units have a cost associated with the activities and Customer should pay for this |
## Contract Terms: Customer v. CM Perspectives

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<tr>
<td>Engineering Changes</td>
<td>- Customer wants to make unlimited changes without much cost because it is used to having its engineering/manufacturing group implement engineering changes as a normal part of the product development/product life cycle</td>
<td>- ECs can drive a profitable CM relationship into the ground; ECs impact costs and schedule. Unless the reason for the EC is within the CM’s responsibilities (i.e., manufacturing process improvement/ problem), CM can’t absorb these added costs without being compensated. &lt;br&gt;- Most ECs are design-, feature-, compatibility-, serviceability- related and not due to manufacturing process changes, so cost/schedule slip impacts should be owned by Customer &lt;br&gt;- CM requires Customer to agree to engineering changes (and impact) and assume responsibility, even if Customer decides to not proceed with any requested engineering changes after CM purchased inventory and expended labor to effectuate the Customer-requested engineering changes.</td>
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## Contract Terms: Customer v. CM Perspectives

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| Best Efforts Standard | Customer wants to use “best efforts” standard on just about any obligation of CM | - CM doesn’t believe there’s a need to include a standard of performance; there’s an implied obligation to perform a contract in good faith and the specifications and CM agreement should sufficiently describe the CM’s obligations.  
- CM never wants to use “best efforts”—standard has been defined in court cases to mean spending every last dime to perform the obligation. CM can’t lose money providing services to the Customer.  
- “commercially reasonable efforts” is more acceptable or redefine “best efforts” to achieve a commercially reasonable standard:  
  - “best efforts” shall not mean efforts which require the performing party to do any act that is commercially unreasonable under the circumstances, to make any capital contribution or to expend any funds other than in payment of reasonable out-of-pocket expenses incurred in satisfying obligations hereunder.” |
# Contract Terms: Customer v. CM Perspectives

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<tr>
<td><strong>BOM</strong></td>
<td>- Customer wants CM to disclose to Customer all details (costs, discounts, benefit; i.e., “open BOM”) of each item included in the BOM and wants CM to pass on to Customer all benefits that CM receives&lt;br&gt;- Customer wants open book audit to verify all prices at the individual component level</td>
<td>- CM wants to disclose pricing for the “bag of parts” on a consolidated basis for the BOM rather than each BOM item individually, to keep the cost benefits that CM has been able to negotiate with the vendors DUE TO THE CM’s EFFORTS.&lt;br&gt;  ○ <em>As an explanation:</em> CM contracts with vendors for parts. To the extent that CM has multiple customers who need the same part, CM may be able negotiate some specific benefits (volume discounts, etc.) CM should be able to keep some of the benefits (i.e., keep the cost differential) of being able to negotiate on behalf of a large number of its customers and get volume discount pricing to obtain large quantities of parts</td>
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## Contract Terms: Customer v. CM Perspectives

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<tr>
<td>Cost Reductions</td>
<td>• Customer wants guaranteed quarterly cost reduction commitments: e.g., “5% per quarter, quarter-on-quarter” as a flat commitment, without consideration of cost impactors (economy, allocation, fuel costs, tax impacts, etc.)&lt;br&gt;• Customer still wants cost reduction commitments even when BOM/product is near End of Life</td>
<td>• CM is willing to discuss cost reductions as a “target” but does not want to be liable for absolute commitments to cost reductions;&lt;br&gt;  o cost reductions may be more likely in the first 12-18 mos. based on process efficiencies, component vendor changes, “popcorn” parts&lt;br&gt;  o component pricing may go up in EOL situations&lt;br&gt;• QBRs are critical to discuss ways of cost improvement</td>
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<td>Cost Sharing</td>
<td>• Customer wants majority of cost savings in a cost sharing program (i.e., share 50%-50% first 60-90 days, then Customer gets 100% thereafter); not much incentive to CM to figure out ways to get costs down</td>
<td>• CM is more likely to find ways to reduce costs if it benefits from cost sharing that is more generous (example: 100% of cost savings to CM the first 90 days, 50%-50% split the next 90 days, thereafter, Customer receives 100% of cost savings)</td>
</tr>
<tr>
<td>PPV (purchase price variance)</td>
<td>This term goes with the BOM description above. Customer wants CM to give Customer all of the benefit of the PPV that the Customer is able to obtain in the manufacturing/supply chain relationship (i.e., if CM is able to get any type of discount on traditional vendor pricing, whether related to a particular customer or a broad range of customers)</td>
<td>CM’s procurement group is often managed based upon how much PPV can be kept within CM to increase the overall profit margin of a CM deal</td>
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# Contract Terms: Customer v. CM Perspectives

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<td>Payment Terms</td>
<td>Customer wants 90-day payment terms (&quot;this is a corporate policy we’ve adopted for all of our vendors&quot;)</td>
<td>CM must have short payment terms, as CM’s investment in performing manufacturing activities also includes buying materials, tooling, etc. CM’s cost of capital is key to being able to stay in a low margin business like the CM business. Thirty (30) day payment terms are key!</td>
</tr>
</tbody>
</table>
| Pricing            | • Customer wants low prices from CM from day 1 of relationship, even lower than Customer was able to manufacture its own products, using same criteria (even if CM takes over Customer plant, people, vendors)  
• Customer wants “most favored nations” pricing  
• Customer wants a provision that allows them to review/audit CM’s “open books” to be sure that they are getting the lowest price | • Customer should pay the price that they are at the end of the day comfortable with paying. If they want to shop around then they should  
• Customer demanding “most favored nations” pricing is due to Customer not wanting to do its own homework  
• CM’s vendors do not want their own vendor component pricing to go to the Customers; this is often subject to an NDA (not the case if the vendor is on Customer’s AVL) |
## Contract Terms: Customer v. CM Perspectives

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<td>Currency Fluctuations</td>
<td>Customer wants a built-in buffer where changes of 5% or greater are addressed</td>
<td>CM has not built in a 5% price fluctuation in the pricing quotes, so CM generally doesn’t want to agree to these scenarios unless CM builds in a 5% pricing bump</td>
</tr>
<tr>
<td>Hubbing</td>
<td>Customer wants CM to fill hub with finished products and for CM to absorb costs of hubbing</td>
<td>CM wants to charge warehousing costs and a distinct provision on when products in hub change title from CM to Customer</td>
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| Third Party Beneficiaries | Customer wants CM to allow third parties (other vendors of Customer) to purchase services or products from CM under the same terms and conditions as the CM-Customer Agreement | • Unless Customer provides a guaranty for the liabilities and duties of the third party, CM will require the third party to undergo credit checks and other credit requirements. Independent contract is required.  
• CM wants additional representations and indemnifications related to IP and product claims from both third party and Customer |
| Contracting/Selling Party(ies) | Customer generally wants the parent company of the CM to be the signatory on the contract and doesn’t much understand or care about any cross-border tax issues based upon where the product sale takes place/point at which Customer takes title | • CM, for tax reasons, needs to be able to specify the appropriate CM selling party (possibly more than 1) depending upon where the manufacturing takes place and the terms of the sale (i.e., EX WORKS, FCA, DDU, etc.); there may be several CM entities involved in the background, depending upon where Customer takes title;  
• generally if CM has tax structuring issues that demand specifying a particular CM entity (or entities) as an contracting party/selling party, |
Amortizing Tooling Costs Over Product Volume

“CM will calculate a per unit contract price adder by amortizing the cost of such tooling over a period of one year from the day of purchase and over the number of units forecast in such year. Customer agrees that the amortization amount per unit shall be added to the price of each unit of Product sold to the Customer. In the event that CM has Product specific tooling related to the Products whose cost has not been completely amortized by: (i) the agreed upon time period; (ii) the respective Product’s end of life (defined as having no forward demand); or (iii) this Agreement is terminated or expires; the Customer shall pay all of any unamortized cost related to such tooling within thirty (30) days of the date of an invoice received from CM.”
Warranties/Remedies

Warranties

• Service Provider warrants for all Products as follows:
• For a period equal to 12 months from the date of manufacture
  – Work has been performed in a professional and workmanlike manner;
  – Products have been manufactured, tested and assembled in accordance with the Specifications and Quality Requirements and are free from defects in workmanship;
  o All Services have been performed in a professional and workmanlike manner, any deliverables provided as a result of such Services shall be free and clear of any liens or encumbrances created by Service Provider. Notwithstanding, Service Provider makes no representations or warranties related to warranties against Intellectual Property or Intellectual Property Rights infringement or ownership., warranty of merchantability or a fitness of purpose.
  o Production processes comply with Environmental Regulation requirements which are contained or referenced in the Specifications.
  o Production Materials specified by Customer shall be utilized in the manufacture of the Products and subject to Service Provider’s Vendor Management activities.
* With regards to materials, Service Provider will transfer to Customer any transferable warranties on the materials provided by the suppliers thereof. Service Provider shall, on behalf of Customer, manage and assist with any return of materials under a material supplier’s warranty.
Warranty Remedies

• Service Provider’s sole obligation and Customer’s sole remedy for any breach of Service Provider’s warranties hereunder will be as follows:

– With respect to Products that do not comply with the above warranties ("Defective Products"), Service Provider will either, at Service Provider’s option, repair or replace the Defective Product at no cost to Customer or its Affiliates. Customer shall return Defective Products after obtaining a RMA number from Service Provider which will be displayed on the shipping container. Service Provider will return all repaired or replaced Products to Customer freight pre-paid.

– With respect to the Services warranty in Section xx, reperform the non-conforming Services until they conform to the applicable warranty. In addition, with respect to any particular Services described in any or more specific Attachments or hereafter agreed by the parties in writing, the applicable remedies set forth in such Attachment(s) or other writing shall apply in addition to the foregoing.
**WARRANTY EXCLUSIONS.** Notwithstanding anything else in this Agreement, the above express limited warranty does not apply to, and Service Provider makes no representations or warranties whatsoever with respect to: (a) Materials; (b) defects resulting from the Specifications or the design of the Products; (c) the compliance of the Product with Environmental Regulations (other than as set forth in Section xxx above); (d) Products that have been abused, damaged, altered or misused by any person or entity after title passes to Customer; (e) first articles, Prototypes, pre-production units, test units; or (f) defects resulting from Customer Tooling (except such defect is proximately caused by a Service Provider’s breach of its obligations with respect to maintaining such Customer Tooling as described in Section xxx); or (g) defects in other Tooling acquired by Service Provider utilizing Customer’s specifications (except to the extent such defect is proximately caused by Service Provider’s breach of its obligations with respect to maintaining such Customer Tooling as described in Section xxx). Customer shall be liable for reasonable costs or expenses incurred by Service Provider related to the foregoing exclusions to Service Provider’s express limited warranty.

**THE REMEDIES CONTAINED IN SECTION XXX. STATE CUSTOMER’S SOLE REMEDIES AND CUSTOMER’S SOLE DAMAGES FOR THE SERVICE PROVIDER WARRANTIES SET FORTH IN SECTION xxx. SERVICE PROVIDER MAKES NO REPRESENTATIONS AND NO OTHER WARRANTIES OR CONDITIONS ON THE PERFORMANCE OF THE WORK, OR THE PRODUCTS, EXPRESS, IMPLIED, STATUTORY, OR IN ANY OTHER PROVISION OF THIS AGREEMENT OR COMMUNICATION WITH CUSTOMER, AND SERVICE PROVIDER SPECIFICALLY DISCLAIMS ANY IMPLIED WARRANTY OR CONDITION OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR NON-INFRINGEMENT.**

**NO CUSTOMER PASS THROUGH.** Customer may elect to provide its own warranties directly to any of its end users or other third parties. However, Customer will not pass through to end users or other third parties the warranties made by Service Provider under this Agreement. Furthermore, Customer will not make any representations to end users or other third parties on behalf of Service Provider.”
Epidemic Failure

“Epidemic Failure.

•Definition of Epidemic Failure. An "Epidemic Failure" shall be deemed to have occurred (as determined by field failure reports, dead on arrival units, Defective Products returned to Service Provider under a Service Provider’s warranty), when the rate of a Service Provider warranted defect which arises out of the same root cause occurs in any lot, batch, or other separately distinguishable group of Product exceeds three percent (3%) of Products delivered to Customer in any three month period or otherwise has or will result in a condition which in the parties’ reasonable opinion presents a potential safety or regulatory issue. For low volume Product shipments (less than 100 units per month), the delivery period can be extended to a rolling six (6) month period, but the 3% defect rate still applies provided there are at least 15 units of Product subject to such defect.

•Both parties commit to address Epidemic Failure with urgency to confirm the condition, analyze root cause, and implement corrective action as required.
• For Epidemic Failure where both parties mutually agree it is a Service Provider workmanship issue (inclusive of Service Provider’s manufacturing processes to Product Specifications), Service Provider will:
  – Bear all reasonable costs of root cause analysis, on site/Hub sort and inspection of Products which are returned to the Service Provider, follow up corrective actions, Product replacement (or repair by mutual agreement), and shipping cost between Customer and Service Provider, and
  – Reimburse Customer ‘true out of pocket’ costs in respect of field service costs related to the Epidemic Failure up to a maximum of [a certain percentage of the CM’s profit on the affected product] per Epidemic Failure occurrence.

• For Epidemic Failure due to any reason other than set forth in clause (c) above, Service Provider will use commercially reasonable efforts to proactively pursue the available remedies on behalf of Customer pursuant to Service Provider's Vendor Management obligations to attempt to ensure that any item of Material that is the cause of an Epidemic Failure is promptly corrected and costs incurred by Customer are absorbed by the responsible vendor. In addition, Customer will reimburse Service Provider for all reasonable costs of root cause analysis, follow-up corrective actions and out-of-scope charges incurred by Service Provider during such Epidemic Failure.

• In the event of a suspected Epidemic Failure, Customer may direct Service Provider to suspend deliveries under accepted Purchase Orders without penalty until the parties are reasonably satisfied that the cause of the Epidemic Failure has been corrected in the affected Product.”
**CM Liability for Components**

“Vendor Management” means interacting in accordance with the requirements of applicable contracts, all third party vendors (both Customer Controlled Vendors and Service Provider Controlled Vendors) producing or delivering Material. “Vendor Management” activities include.... (vii) attempting to incorporate by reference in Service Provider’s contracts or purchase orders to Customer Controlled Vendors any terms and conditions negotiated by Customer and provided to Service Provider and extending to Customer all of those terms which are transferable; and (viii) to the extent not included in (vii) above and where allowable, obtain and pass through to and for the benefit of Customer the following vendor obligations warranties and indemnifications with regard to all other Materials (using Customer's form of vendor approval, if requested).... “Vendor Management” also includes proactively pursuing available remedies on behalf of Customer. However, it does not include instituting legal proceedings in the name of Customer, or assuming any vendor liability related to vendor's defective Materials on behalf of vendor nor does it include settling any disputes other than facilitating the resolution of any pass-through rights from vendors for the benefit of Customer. Service Provider may not limit Customer’s rights, create any admission of liability by Customer or create new obligations for Customer with any third party.”
**Obsolete Material**

“In the event of a complete or partial termination by either Party, rescheduling or cancellation of a forecast or Purchase Order by Customer, or the termination of all or any part of this Agreement, or any other event, including a change in Specifications or an engineering change, which results in any Unique Inventory which Service Provider has purchased or issued a purchase order to the Material manufacturer and which is no longer required to manufacture Product, such Unique Inventory shall be considered “Obsolete Material” and Customer shall be notified of same. Customer shall review and approve in writing all Obsolete Material identified by Service Provider; provided that Customer’s approval will not be unreasonably withheld or delayed. To be considered for Obsolete Material, Unique Inventory must be packaged in original vendor packaging and in good and usable condition. Customer shall have ten Business Days to confirm whether material is Obsolete Material. In the event Customer fails to respond within ten Business Days, such Material shall be deemed Obsolete Material. Obsolete Material will be dealt with and Customer shall be liable for such Obsolete Material pursuant to this Section xxx.”
**Excess Material**

“If at the end of any quarter, the demand for any Unique Inventory on the Bill of Materials for a Product, based on the current 12-month forecast as provided by Customer, does not project consumption of the Unique Inventory that Service Provider owns or has committed to purchase within the following six months, then such Unique Inventory shall be deemed “Excess Material,” unless otherwise mutually agreed in writing by the Parties. Customer shall provide Service Provider with purchase orders for the price of any such Excess Material. Pricing for Excess Material shall be in accordance with the then-current Material price list. In the event Customer stores such Excess Material at Service Provider’s facility as consigned stock and it later becomes Obsolete Material, then Customer will pay Service Provider the associated Material Overhead Cost and profit for such Obsolete Material.”
Supply Chain Practices

Unless otherwise agreed to in writing between the parties, Service Provider will purchase all Material required to manufacture Products in the quantity set forth in Customer's Purchase Order. Where Customer has agreed specific terms and conditions with Customer Controlled Vendors, Service Provider will, as part of Vendor Management, procure Material on behalf of Customer under the terms and conditions of the Customer contracts with the Customer Controlled Vendors. Subject to restrictions in this Section, Customer's accepted Purchase Orders and forecast will constitute Service Provider’s authorization to purchase, without Customer’s prior approval (except as set forth below), Material based on Material vendor lead times when the Purchase Orders are placed, as well as vendor’s minimum order quantities and Vendor Economic Order Quantities for Materials specified on the costed BOM from Customer Controlled Vendors and Service Provider Controlled Vendors in such quantities as necessary to support Customer’s production requirements as provided in Customer’s forecast and the demand flexibility requirements of Section xxx. This non-binding forecast shall be used by Service Provider for planning purposes and to begin procuring Material, but it is not a commitment by Customer to procure the volume of Products in the forecast.

• Service Provider shall obtain written approval from Customer prior to purchasing or committing to purchase any Material in excess of the amount needed to manufacture the volume of Products forecasted by Customer, including without limitation Economic or Minimum Order Quantities.

• Service Provider shall use commercially reasonable, prudent Material management practices, including but not limited to, Service Provider managed inventory methodologies to shorten Material lead times and minimize Customer’s Material liability."
Pricing, Changes

“Fees; Changes; Taxes.

- The fees will be agreed by the parties and will be indicated on the purchase orders issued by Customer and accepted by Service Provider. The initial fees shall be as set forth on the Fee List attached hereto and incorporated herein as Exhibit xxx (the “Fee List”). If a Fee List is not attached or completed, then the initial fees shall be as set forth in purchase orders issued by Customer and accepted by Service Provider in accordance with the terms of this Agreement.

- Customer is responsible for additional fees and costs due to: (a) changes to the Specifications; (b) failure of Customer or its subcontractor to timely provide sufficient quantities or a reasonable quality level of Customer Controlled Materials where applicable to sustain the production schedule; and (c) any pre-approved expediting charges reasonably necessary because of a change in Customer's requirements.

- The fees may be reviewed periodically by the parties. Any changes and timing of changes shall be agreed by the parties, such agreement not to be unreasonably withheld or delayed. By way of example only, the fees may be increased if the market price of fuels, Materials, equipment, labor and other production costs, increase beyond normal variations in pricing or currency exchange rates as demonstrated by Service Provider.

- All fees are exclusive of federal, state and local excise, sales, use, VAT, and similar transfer taxes, and any duties, and Customer shall be responsible for all such items. This subsection does not apply to taxes on Service Provider's net income.”
Currency Exchange Variations

“The Fees List will be based on the exchange rate(s) for converting the purchase price for Inventory denominated in the Parts Purchase Currency(ies) into the Functional Currency. The fees will be adjusted, on a monthly basis based on changes in the Exchange Rate(s) as reported on the last business day of each month, for the following month to the extent that such Exchange Rates change +/- .75% from the prior month. “Exchange Rate(s)” is defined as the closing currency exchange rate(s) as reported on Reuters' page FIX on the last business day of the current month prior to the following month. “Functional Currency” means the currency in which all payments are to be made pursuant to Section xxx below. “Parts Purchase Currency(ies)” means U.S. Dollars, Japanese Yen and/or Euros to the extent such currencies are different from the Functional Currency and are used to purchase inventory needed for the performance of the Work forecasted to be completed during the applicable month.”
**Indemnification Provisions**

“Customer shall defend Service Provider against, and shall indemnify Service Provider for Indemnified Liabilities arising from, any:

- Claims that the Products infringe any third party Intellectual Property Rights, private rights or contractual rights, except to the extent the Claims would not have arisen but for a reason for which Service Provider is obligated to indemnify Customer as described in Section xxx below; and

- Claims of personal injury (including death) or damage to any person or tangible property caused, or alleged to be caused by: (A) the sale or use of a Product, except to the extent that such damage or injury is caused by any of the factors for which Service Provider would indemnify Customer as described in Section xxx.; and

- Claims that the Products did not comply with Environmental Regulations.
Service Provider shall defend Customer and shall indemnify Customer for Indemnified Liabilities arising from:

- Claims that Service Provider’s Intellectual Property or production or testing processes not mandated or provided by Customer, or the use of any of the foregoing in performance of Work or Services, infringes any third party Intellectual Property Rights, private rights or contractual rights, except to the extent the Claims would not have arisen but for the Specifications;

- Claims of personal injury (including death) or damage to any person or tangible property caused, or alleged to be caused by: (A) the Work or Services; (B) a Product, to the extent that such damage or injury is alleged to have been caused by a breach of Service Provider’s warranties set forth in Section xxx(i) and (ii) or the applicable warranty as it applies to Services; except in all cases in subclauses (A) and (B) above in this xxx to the extent the Claims or Indemnified Liabilities would not have arisen but for: (X) Customer or its Affiliates’ gross negligence or willful misconduct; or (Y) a reason for which Customer is obligated to indemnify Service Provider as described in Section xxx above;
Negotiated Clauses- Examples

**IP Licenses**

"Customer License Grant. Customer grants Service Provider a non-exclusive license during the Term of this Agreement to use certain of Customer's patents, trade secrets and other intellectual property solely as is necessary to perform Service Provider's obligations under this Agreement and solely for the benefit of Customer. Solely for the performance of this Agreement, and as instructed by Customer, Service Provider shall be entitled to use the logo, name, trademark, trade name or service mark, (collectively, “Name or Mark”) of Customer as well as any third party intellectual property available from Customer or its Affiliates that is needed for Service Provider to perform the Work hereunder. If Customer requires that Service Provider incorporate any third party logos or trademarks or any other third party intellectual property into the Product or packaging, then Customer will be responsible for obtaining any third party consents or approvals required for Service Provider to do so. Service Provider shall be responsible for (i) having all necessary rights to its Background Technology to enable it to perform the Work, and (ii) obtaining any third party licenses that it needs to perform its manufacturing services (except as set forth in the immediately following sentence), including without limitation, any third party manufacturing process licenses. Notwithstanding anything above to the contrary, Customer or its Affiliates shall provide to Service Provider any third party licenses necessary for Service Provider to manufacture those portions of the Products that are unique to Customer. "Service Provider Background Technology" means any and all manufacturing processes and manufacturing process improvements (including any intellectual property rights existing therein) that are owned by or licensed to Service Provider as of the Effective Date of this Agreement, but excluding any Customer technology and intellectual property."
“Service Provider License Grant. Service Provider hereby grants Customer a perpetual, non-revocable, non-exclusive, non-royalty bearing license to use Service Provider’s Background Intellectual Property (and associated Intellectual Property Rights thereto) to the extent it is necessary or desirable for Customer’s use of Foreground Intellectual Property owned by Customer for the purpose of manufacturing by Customer directly but not indirectly through any third party, distributing (either directly or indirectly through Distribution Partners), repairing Products or successors thereto by Customer directly but not indirectly through any third party.”
Typical MOU

• Service Provider and Customer have agreed to proceed with a manufacturing relationship under the terms of this Memorandum of Understanding. Service Provider shall manufacture the required products per Customer’s purchase orders. Customer agrees to provide Service Provider with a rolling twelve (12) month forecast of anticipated product requirements so as to allow Service Provider to procure the necessary materials, in accordance with lead-times, to meet Customer’s product requirements. Service Provider shall order materials with sufficient lead time to procure, kit and manufacture the product demand requirements as stated in the forecast provided by Customer. Customer agrees not to change any forecasted demand or purchase orders within a thirty (30) day period prior to the stated delivery date so as not to interrupt the actual kitting and manufacturing of the products.
Negotiated MOU - Example

- Customer understands that Service Provider will rely on Customer’s purchase orders and forecasts to order and purchase materials necessary to fulfill such purchase orders, forecasts, and any Customer requested increase or flexibility to increase the quantity of products ordered or purchased. Orders issued for materials may be non-cancelable with suppliers and materials received by Service Provider non-returnable to suppliers. Service Provider shall obtain Customer’s prior written consent before purchasing materials which, at the time of procurement, are identified by the supplier thereof as non-cancelable or non-returnable materials. Accordingly, once Service Provider has received or ordered materials in support of Customer’s purchase orders or forecasts, Customer will be liable for these materials if such materials are not consumed as and when contemplated by the purchase orders or forecasts Service Provider relied upon to order or purchase such materials. Customer acknowledges that this liability may include (i) any unconsumed minimum or economic order quantities of materials, which may exceed Customer’s actual forecast or purchase order demand, (ii) materials ordered or purchased by Service Provider to support Customer’s requested increase, or flexibility to increase, the quantity of products ordered or forecasted, and (iii) Service Provider’s quoted and agreed to total material mark-up on materials. Service Provider and Customer will review these liabilities upon the request of either party. Without limiting the foregoing, Service Provider will be entitled to charge Customer an inventory management fee of two percent (2%) of material costs per month, in the event Service Provider has held material purchased as provided above for more than sixty (60) days. If the materials are held by Service Provider for more than one hundred eighty (180) days, Service Provider will be entitled to invoice and ship such materials to Customer. Invoices issued by Service Provider in connection with Customer’s liability for such materials will be paid via electronic funds transfer by Customer no later than thirty (30) days following the date of Service Provider’s invoice and under other payment terms and conditions provided below. Service Provider will use all reasonable efforts to minimize Customer’s liability by returning these materials to suppliers, canceling orders with suppliers, or using these materials to manufacture product for other Service Provider customers whose demand reflects a current need for such materials.
Negotiated MOU - Example

- Product manufactured by Service Provider will be quoted and shipped Ex Works (Incoterms 2000) Service Provider’s manufacturing facility. Prices for product quoted by Service Provider will not include, and Customer agrees to pay, any sales, use, excise, value added or similar taxes imposed on the sale of the products to or performance of any services for Customer, excluding any taxes on Service Provider’s income. All payments shall made via electronic fund transfer and received by Service Provider in US Dollars no later than thirty (30) days following the date of Service Provider’s invoice. If Customer believes there are any discrepancies in Service Provider’s invoices, Customer shall notify Service Provider no later then ten (10) days after the date of invoice. Invoices not paid within thirty (30) days of the date thereof will be subject to an interest charge equal to the lesser of 1.5% per month or the highest rate allowed by law. Customer acknowledges that the above payment terms, and any other credit terms, limits, or vehicles granted by Service Provider to Customer during the course of the performance of this Agreement, will be subject to periodic review and modification by Service Provider at any time at its discretion. In addition, Customer acknowledges that Service Provider may request, and Customer shall provide to Service Provider promptly upon any such request, financial information to verify Customer’s financial condition. Service Provider will maintain any such information provided by Customer to Service Provider confidential in accordance with the terms of the non-disclosure agreement in place between the parties at the time of disclosure.
Negotiated MOU - Example

• The warranty offered by Service Provider with respect to the products manufactured for Customer will be a limited warranty that the products will be free from defects in workmanship performed by Service Provider for a period of twelve (12) months from the date of shipment where the workmanship does not conform to the manufacturing specifications agreed upon in writing by Service Provider and Customer. Service Provider’s obligation with regard to products returned under warranty to Service Provider will be limited to either repair or replacement by Service Provider, at Service Provider’s cost and option. With respect to materials, Service Provider will transfer to Customer any transferable materials warranties received from the materials supplier. If materials are returned under supplier’s warranty, Service Provider will, on Customer’s behalf and without additional charge, manage the return of any such materials to the supplier for repair or replacement. EXCEPT AS PROVIDED IN THIS PARAGRAPH, SERVICE PROVIDER MAKES NO WARRANTIES WITH RESPECT TO THE PRODUCTS OR ITS SERVICES, EXPRESSED OR IMPLIED, INCLUDING ANY IMPLIED WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR ANY IMPLIED WARRANTIES ARISING FROM A COURSE OF PERFORMANCE OR DEALING, OR TRADE USAGE. IN NO EVENT, WHETHER AS A RESULT OF BREACH OF CONTRACT, WARRANTY, TORT (INCLUDING NEGLIGENCE), STRICT LIABILITY, OR OTHERWISE, SHALL EITHER PARTY OR ITS AFFILIATES BE LIABLE FOR ANY INCIDENTAL, EXEMPLARY, INDIRECT OR CONSEQUENTIAL DAMAGES, WHETHER OR NOT THE PARTY ITS AFFILIATES WERE INFORMED OR AWARE OF THE POSSIBILITY OF SUCH DAMAGES OR LOSS AND NOTWITHSTANDING THE FAILURE, OR ESSENTIAL PURPOSE, OF ANY REMEDY.
• In the event the parties do not have a confidentiality agreement specifically addressing the exchange of information contemplated herein, the parties shall then use reasonable efforts to prevent the unauthorized disclosure of any Confidential Information exchanged between the parties; provided that such efforts are not less than those used to protect its own Confidential Information. Confidential Information is defined as all information relating to either party’s business that is exchanged under this Agreement. Confidential Information shall not include information that is: (a) generally available to or known to the public, (b) previously known to the recipient without any obligation of confidentiality, (c) independently developed by the recipient without any use of the other party’s Confidential Information, (d) lawfully disclosed to the recipient by a third party under no obligation of confidentiality, or (e) disclosed pursuant to a valid court order or required by a judicial court of competent jurisdiction.
Customer acknowledges that Service Provider will be manufacturing product in conformance with Customer approved designs and/or specifications. Therefore, Customer agrees that it will be responsible for any claims, costs or liabilities arising from the sale or use of the products manufactured by Service Provider in accordance with these designs or specifications and will indemnify, defend and hold Service Provider harmless therefrom. Service Provider shall indemnify and hold Customer harmless from any third party claims, costs or liabilities arising from Service Provider’s manufacturing processes which infringe any intellectual property rights of a third party.
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