

CHOREY, TAYLOR & FEIL BULLETIN:

KEY ISSUES FACING MANUFACTURERS AND DISTRIBUTORS IN THE CURRENT BUSINESS ENVIRONMENT

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The business climate in North America presents continuing challenges for manufacturers. Many manufacturers and distributors have been affected by the sharp decline in the housing market, which is now affecting commercial construction. As this is being written, the credit markets are in turmoil, with Lehman Brothers having declared bankruptcy and the federal government having rescued insurance giant AIG. At the same time, business opportunities still remain, particularly in the middle market, and those who weather the current financial storm can look forward to better days ahead.

Based on our representation of manufacturers and distributors, as well as other clients, here are some of the key issues facing manufacturers and distributors in the current environment:

1. **Getting Paid.** Getting paid for goods and services can be a challenge in the best of times, and is certainly a vitally important issue with tight credit and declining sales.

Manufacturers and distributors must be vigilant in monitoring payment by their customers. Manufacturers and distributors should revisit their standard payment terms and may wish to require more money to be paid at the time of the order or upon delivery. Payment security, including letters of credit, should be considered. In the event payment appears doubtful or even slower than usual, a manufacturer or distributor may wish to demand adequate assurance of performance. It is important to be proactive with customers regarding past due amounts and not to let debts linger or grow larger. It is usually more effective and ultimately less expensive to involve counsel sooner rather than later regarding troublesome accounts, particularly when the customer is showing significant signs of financial duress.

2. **Careful Review of Commercial Terms and Conditions.** In challenging financial times, customers may be more aggressive in negotiating commercial terms and conditions. On the theory that it is a "buyer's market," customers may try to force manufacturers and distributors to grant extended warranties, indemnities, or other provisions that may substantially shift the allocation of risk associated with a transaction. It is very important for manufacturers and distributors to know what they are signing and to understand the risk and obligations they are being asked to assume. Manufacturers and distributors should not assume such provisions are non-negotiable. Often, the key is simply getting to a person with authority in the customer's organization. Watch out for form terms and conditions which may be printed on an order confirmation, or even referenced on a website. Those form "T&Cs" are not just "legal mumbo jumbo," can substantially affect your

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company's legal rights, and may become binding if no objection is made. Again, being proactive is the key – by understanding the potential exposure created by expanded terms and conditions, a manufacturer can balance the damage caused by making a sale with risky terms against the cost of making no sale at all.

3. NDA Mania. Non-disclosure agreements (or “NDAs”) are becoming more and more common in business transactions. NDAs are intended to protect the confidential business information and trade secrets of the parties. When properly structured, NDAs can be very useful and protect the interests of both parties. Many NDAs contain similar provisions, but they are *not* all the same. Many forms may protect only the customer, or may contain inappropriate provisions that affect the intellectual property rights of a party. Since there are a number of features that are variable within an NDA (like whether it needs to be mutual, how long the protections should last, and to what should the protections apply), there is no “one size fits all” document. An aggressively drafted NDA from a customer could actually impair a manufacturer's ability to sell future product lines. Clients sometimes see us after they have signed an NDA with troublesome or inappropriate provisions. Although it may be possible to re-negotiate or amend such agreements, an NDA should be treated as any other important agreement. That means the NDA should be fully understood *before* it is signed.
4. Insurance Coverage. A company should review its insurance program regularly with its broker or other professionals familiar with insurance coverage. However, coverage is particularly important in a difficult financial environment. It is also important to consider the financial strength of the insurers and their reputation for fairly handling claims. If an insurer denies a claim or reserves its rights, counsel should be consulted. An early consultation or review normally increases the chances for a better outcome. Brokers and other professionals familiar with insurance coverage should be consulted in connection with a company's contractual undertakings to make sure that the insurance protection in place adequately matches the risks being assumed contractually.
5. Dispute Resolution. Unfortunately, rocky financial times lead inexorably to a greater frequency of disputes. Many commercial agreements contain dispute resolution provisions that provide, for example, that any claims will be resolved only in the courts of a certain jurisdiction or will be resolved by binding arbitration. Arbitration is a process in which a dispute is resolved by an arbitrator (often a lawyer) or a panel of arbitrators. In most instances, such provisions will be found enforceable, particularly in a commercial context. Although dispute resolution provisions can substantially affect the rights of the parties, they are often overlooked by business people during negotiations. Again, it is important to understand such provisions before entering into an agreement, particularly when, as a result of the current conditions, disputes are more likely.

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