# **APPENDIX A:** **Contract Negotiation and Drafting Exercise**

**A.1 Buyer’s Instructions**

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**A.1 Buyer’s Instructions**:

You are the head of a division of an electronics company, Honeycrisp, headquartered in St. Paul, Minnesota, and you will be releasing a new cell phone. In order to deliver long battery life but compact size, you will utilize lithium batteries in your device. You will be meeting with the CEO of a lithium battery manufacturer, Libatt, to discuss having them supply 100,000 lithium batteries for you (one for each cell phone). In preparation for this meeting, you have collected some important information from within your company.

Your company has determined (with absolute certainty) that you will be able to sell all of these cell phones for $100 each. With the exception of the battery costs, all other costs (including inputs, marketing, etc.) will total $60 for each device. Consequently, you could generate a profit from your cell phones, as long as the total cost (including any shipping charges that you pay, plus any expected damage payments that you are responsible) for all batteries is below four million dollars ($4,000,000).

One of the key concerns with lithium batteries is the possibility that the batteries may catch fire or explode. There have been a number of recalls for lithium batteries for laptops. In 2006, Dell, Apple, Toshiba, and Lenovo recalled lithium laptop batteries due to possible fire or explosions.[[1]](#footnote-1) Hewlett Packard recalled lithium batteries in 2009.[[2]](#footnote-2) Lithium battery recalls have not been limited to laptop computers either. In August 2010, Apple recalled iPod nanos due to lithium batteries, because they could “overheat and prevent the iPod nano from working and deform it.”[[3]](#footnote-3)

These problems are caused by small metal particles that sometimes show up in the lithium solution inside a battery cell. When heated significantly, such as during extended use of a battery, these metal particles may cut into the separator between battery cells. This causes a short circuit, which can lead to a fire or explosion.[[4]](#footnote-4)

You face a major problem in buying these batteries from Libatt. You have heard that Libatt uses two different techniques: one essentially eliminates the risk of fire or explosion, while this risk remains for the other. Your problem is that, once manufactured, you will be unable to determine which technique was used for your batteries (the differences are within the sealed liquids, and you may not trust the external markings). Your engineers have constructed estimates of possible fires, explosions, and monetary damages that would result from these. These are included in the table below. You should consider whether you might want some sort of legal protection from Libatt when you cannot tell which technique has been used. (What legal concept would protect you in case of a fire or explosion?)

You are expecting to have a good product launch, but it is essential for the batteries to be available to your Shakopee, Minnesota manufacturing facility by November 21st (**you may lose all sales if you miss this deadline** – i.e. your revenues will be **zero!**).

You also have information about your exclusive shipping contractor, Consolidated Express (which is the only one you are allowed to contract with). The cost for shipping 100,000 batteries from anywhere within the United States will be $100,000. Libatt may use another shipper.

Furthermore, as you can probably tell, you are extremely busy, and do not want to deal with the long delays and cost of litigation. You would prefer using an alternative, if any dispute arose. You have heard that the American Arbitration Association can provide a fair and unbiased alternative procedure.

Below is a table with some data provided by your company, and some calculations that you should do to help in your negotiation:

|  |  |  |
| --- | --- | --- |
| Total Revenues from New cell phones, if you receive batteries prior to October 21 |  | $10,000,000 |
| Total Costs from all other Expenses |  | $6,000,000 |
| Expected number of overheating incidents if lesser technique used (for 100,000 batteries) |  | 30 |
| Expected number of overheating incidents if better technique used (for 100,000 batteries) |  | 0 |
| Average Expected Damages to Consumers from each Overheating Incident |  | $100,000 |
| Total Expected Damages to Consumers if Lesser Technique Used | #1 |  |
| Proposed “Low” Total Price for 100,000 batteries |  | $500,000 |
| Total Profits if the only costs you pay are the “Low” price for the batteries (no shipping and no damages due to overheating) | #2 |  |
| Total Profits if the only costs you pay are the “Low” price for the batteries and damages (assume that the lesser technique is used) (no shipping costs) | #3 |  |
| Total Profits with “Low” price if you pay for shipping but there are no damages (assume that the better technique is used) | #4 |  |
| Total Profits with “Low” price if you pay for both shipping and damages (assume that the lesser technique is used) | #5 |  |
| Proposed “High” Total Price for 100,000 batteries |  | $3,800,000 |
| Total Profits if the only costs you pay are the “High” price for the batteries (no shipping and no damages due to overheating) | #6 |  |
| Total Profits if the only costs you pay are the “High” price for the batteries and damages (assume that the lesser technique is used) (no shipping costs) | #7 |  |
| Total Profits with “High” price if you pay for shipping but there are no damages (assume that the better technique is used) | #8 |  |
| Total Profits with “High” price if you pay for both shipping and damages (assume that the lesser technique is used) | #9 |  |

**Assignment**:

You are going to attempt to negotiate a sales contact for purchasing batteries. You must do the following:

1. Complete the table, questions #1 - #9. In doing these calculations, you will use a “low price” for some and a “high price” for others. Comparing profits with different prices lets you see what happens to your profits as you change prices. That will help when you are bargaining over different prices. Record your calculations in Canvas for the “pre-class assignment”.
2. Use class discussion / notes / PowerPoint to figure out how you could phrase a shipping clause.
3. Use class discussion / notes / PowerPoint to figure out what sales law concept could protect you from the risk of the lesser-technique batteries. How might you write a clause to ensure that concept would apply to your contract? In doing so, use legal terms from class with explanations that both you and your partner would understand. Also, make sure that this clause refers to the specific facts of your situation.
4. Research a standard clause you might want to use in order to apply the process of the “American Arbitration Association.”
5. Come to class Tuesday ready to negotiate.
   1. First negotiate over the three clauses (B-D).
   2. Then negotiate price for the batteries.
6. Draft your contract, and execute it.
   1. Fill out the relevant blanks.
   2. Fill out the three clauses you negotiated.
   3. Don’t forget to \_\_\_\_\_\_\_!

**A.2 Seller’s Instructions**:

You are the CEO of a lithium battery manufacturer headquartered in Minneapolis, Libatt. A large electronics company, Honeycrisp, has approached you about supplying batteries for its new cell phone. These phones normally sell for around $100 - $150. You know that they are looking to purchase 100,000 batteries for their cell phone. You know that they have other costs in producing these devices, but you would like to keep as large a share of their sales revenues for yourself. You are preparing to meet with the division head in charge of this new product. You have collected some important information from within your company.

One of the key concerns in lithium battery manufacturing is the possibility that the batteries may catch fire or explode. There have been a number of recalls for lithium batteries for laptops. In 2006, Dell, Apple, Toshiba, and Lenovo recalled lithium laptop batteries due to possible fire or explosions.[[5]](#footnote-5) Hewlett Packard recalled lithium batteries in 2009.[[6]](#footnote-6) Lithium battery recalls have not been limited to laptop computers either. In August 2010, Apple recalled iPod nanos due to lithium batteries, because they could “overheat and prevent the iPod nano from working and deform it.”[[7]](#footnote-7)

These problems are caused by small metal particles that sometimes show up in the lithium solution inside a battery cell. When heated significantly, such as during extended use of a battery, these metal particles may cut into the separator between battery cells. This causes a short circuit, which can lead to a fire or explosion.[[8]](#footnote-8)

In one of your older facilities in Worcester, Massachusetts, you use a manufacturing process that leaves some of these particles in the lithium battery solution. However, in a new facility in Corvallis, Oregon, you have developed an advanced and costly manufacturing method that virtually eliminates these particles, leading to an essentially zero chance of fire or explosion. Below, you will find a table showing your engineers’ calculations of the manufacturing costs of your batteries in each facility; along with their extremely accurate estimates of possible fires, explosions, and monetary damages that would result from these.[[9]](#footnote-9) If these damages are high, your profits will be significantly lower if you agree to be responsible for paying them. On the other hand, due to the sealed nature of the batteries and a possible distrust of your external markings, your customer may be unable to determine which process you have used.

You can have the batteries delivered within three weeks of the order.

You also have information about your exclusive shipping contractor, Federal Parcel Service (which is the only one you are allowed to contract with). The cost for shipping the batteries from either facility with FPS will be $200,000. Honeycrisp may use another shipper.

Furthermore, as you can probably tell, you are extremely busy, and do not want to deal with the long delays and cost of litigation. You would prefer using an alternative, if any dispute arose. You have heard that the American Arbitration Association can provide a fair and unbiased alternative procedure.

Below is a table with some data provided by your company, and some calculations that you should do to help in your negotiation:

|  |  |  |
| --- | --- | --- |
| Total Manufacturing Cost if use Massachusetts Facility |  | $1,000,000 |
| Total Manufacturing Cost if use Oregon Facility |  | $1,900,000 |
| Expected number of overheating incidents if lesser technique used (for 100,000 batteries) |  | 30 |
| Expected number of overheating incidents if better technique used (for 100,000 batteries) |  | 0 |
| Average Expected Damages to Consumers from each Overheating Incident |  | $100,000 |
| Total Expected Damages to Consumers if Lesser Technique Used | #1 |  |
| Proposed “High” Total Price for 100,000 batteries |  | $5,000,000 |
| Total Profits with “High” price if Use Massachusetts facility, you are not responsible for costs other than manufacturing ones (no shipping nor damage costs) | #2 |  |
| Total Profits with “High” price if Use Massachusetts facility, you are responsible for damages to consumers but not shipping costs | #3 |  |
| Total Profits with “High” price if Use Massachusetts facility, you are responsible for damages to consumers and also shipping costs | #4 |  |
| Total Profits with “High” price if Use Oregon facility, you are not responsible for costs other than manufacturing ones (no shipping nor damage costs) | #5 |  |
| Total Profits with “High” price if Use Oregon facility, you are responsible for damages to consumers but not shipping costs | #6 |  |
| Total Profits with “High” price if Use Oregon facility, you are responsible for damages to consumers and also shipping costs | #7 |  |
| Proposed “Low” Total Price for 100,000 batteries |  | $2,000,000 |
| Total Profits with “Low” price if Use Massachusetts facility, you are responsible for damages to consumers but not shipping costs | #8 |  |
| Total Profits with “Low” price if Use Oregon facility, you are responsible for damages to consumers but not shipping costs | #9 |  |

**Assignment**:

You are going to attempt to negotiate a sales contact for selling batteries. You must do the following:

1. Complete the table, questions #1 - #9. In doing these calculations, you will use a “low price” for some and a “high price” for others. Comparing profits with different prices lets you see what happens to your profits as you change prices. That will help when you are bargaining over different prices. Record your calculations in Canvas for the “pre-class assignment”.
2. Use class discussion / notes / PowerPoint to figure out how you could phrase a shipping clause.
3. Use class discussion / notes / PowerPoint to figure out what sales law concept could force you to produce the batteries via the better-technique. How might you write a clause to ensure that concept would apply to your contract? In doing so, use legal terms from class with explanations that both you and your partner would understand. Also, make sure that this clause refers to the specific facts of your situation.
4. Research a standard clause you might want to use in order to apply the process of the “American Arbitration Association.”
5. Come to class Thursday ready to negotiate.
   1. First negotiate over the three clauses (B-D).
   2. Then negotiate price for the batteries.
6. Draft your contract, and execute it.
   1. Fill out the relevant blanks.
   2. Fill out the three clauses you negotiated.
   3. Don’t forget to \_\_\_\_\_\_\_!

**A.3 Contract Negotiation: Sales Contract with Blanks**

**SALES CONTRACT**

SOLD BY \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

TO \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

QUANTITY \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

DESCRIPTION \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

PRICE \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

DATE OF ARRIVAL \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

B. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

C. \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

D.\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

DATE: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

Seller Buyer

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

Title Title

**A.4 Seller’s Pre-negotiation Quiz** (correct responses in **bold**)

#1 Total Expected Damages

$100,030



$100 thousand



**$3 million**



$30



#2 Total Profits

$1 million



**$4 million**



$3.9 million



$5 million



#3 Total Profits

loss of $3 million



**$1 million**



$4 million



$3.5 million



#4 Total Profits

loss of $2.8 million



$3.8 million



$1 million



**$800 thousand**



#5 Total Profits

loss of $2.9 million



$3.4 million



**$3.1 million**



$6.4 million



#6 Total Profits

$3.2 million



$3.1 million



$6.2 million



loss of $2.8 million



**A.4 Seller’s Pre-negotiation Quiz** (correct responses in **bold**) (continued)

#7 Total profits

$3.1 million



$200 thousand



**$2.9 million**



loss of $3 million



#8 Total Profits

**loss of $2 million**



loss of $2.9 million



$1 million



$100 thousand



#9 Total Profits

$2 million



$200 thousand



loss of $2.9 million



**$100 thousand**



**A.5 Buyer’s Pre-negotiation Quiz** (correct responses in **bold**)

#1 Total Expected Damages

$100,030



$30



$100 thousand



**$3 million**



#2 Total Profits

$4 million



$9.5 million



**$3.5 million**



$500 thousand



#3 Total Profits

$4 million



loss of $2.8 million



**$500 thousand**



$3.5 million



#4 Total Profits

$500 thousand



loss of $2.8 million



$3.5 million



**$3.4 million**



#5 Total Profits

$3.4 million



**$400 thousand**



loss of $2.9 million



$6.4 million



#6 Total Profits

$6.2 million



$3.2 million



**$200 thousand**



loss of $2.8 million



**A.5 Buyer’s Pre-negotiation Quiz** (correct responses in **bold**) (continued)

#7 Total profits

$200 thousand



$3.2 million



**loss of $2.8 million**



$6.2 million



#8 Total Profits

$3.1 million



$6.1 million



**$100 thousand**



loss of $2.9 million



#9 Total Profits

**loss of $2.9 million**



$3.1 million



$100 thousand



$200 thousand



**A.6 Contract Negotiation Results Scoring**

Results when no pre-quiz required:

|  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Team | Price | Shipping Costs for buyer | Uncertainty in shipping | Shipping Costs for Seller | Damages (which occur if no warranty) | Arbitration (maybe mediation for lesser benefit) | Transaction Costs due to Unclear arbitration clause | Transaction Costs due to Unclear warranty | Profit for Seller | Profit for Buyer | Joint Profits |
| A | $2,900,000 | 100000 | ($10,000) |  |  | $50,000 |  | -30000 | $1,010,000 | $1,010,000 | $2,020,000 |
| B | $2,900,000 | 100000 | -3500 |  |  | $50,000 |  | -20000 | $1,026,500 | $1,026,500 | $2,053,000 |
| C | $2,500,000 | 100000 | -5000 |  |  | $50,000 |  | -5000 | $640,000 | $1,440,000 | $2,080,000 |
| D | $2,900,000 | 100000 | -1000 |  |  | $50,000 |  | -10000 | $1,039,000 | $1,039,000 | $2,078,000 |
| E | $7,400,000 |  | -10000 | 200000 |  | $50,000 |  | -20000 | $5,320,000 | ($3,380,000) | $1,940,000 |
| F | $4,000,000 |  | -5000 | 200000 |  | $50,000 |  | -20000 | $1,925,000 | $25,000 | $1,950,000 |
| G | $2,900,000 |  | -1000 | 200000 |  | $15,000 |  | -25000 | $789,000 | $1,089,000 | $1,878,000 |
| H | $2,900,000 | 100000 | -10000 |  |  | $50,000 | -5000 | -25000 | $1,010,000 | $1,010,000 | $2,020,000 |
| I | $2,900,000 |  | -10000 | 200000 |  | $50,000 | -5000 | -20000 | $815,000 | $1,115,000 | $1,930,000 |
| J | $2,900,000 |  | -10000 | 200000 |  | $50,000 |  | -10000 | $830,000 | $1,130,000 | $1,960,000 |
| K | $3,000,000 | 100000 |  |  |  | $50,000 |  | -5000 | $1,145,000 | $945,000 | $2,090,000 |
| L | $2,900,000 |  | -10000 | 200000 |  | $50,000 |  | -5000 | $835,000 | $1,135,000 | $1,970,000 |
| M | $2,900,000 | 100000 | -10000 |  |  | $50,000 |  | -20000 | $1,020,000 | $1,020,000 | $2,040,000 |
| N | $2,250,000 | 100000 |  |  |  | $50,000 |  | -1000 | $399,000 | $1,699,000 | $2,098,000 |
| O | $3,000,000 | 100000 | -500 |  |  | $15,000 |  | -10000 | $1,104,500 | $904,500 | $2,009,000 |
| P | $2,900,000 | 100000 |  |  |  | $50,000 |  | -1000 | $1,049,000 | $1,049,000 | $2,098,000 |

Results with pre-quiz required:

|  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Team | Price | Shipping Costs for buyer | Uncertainty in shipping | Shipping Costs for Seller | Damages | Arbitration | TC - Arb | TC - Unclear warranty | Profit for Seller | Profit for Buyer | Joint Profits |
| A | $2,850,000 | $100,000 | ($5,000) |  |  | $40,000 |  | ($10,000) | $975,000 | $1,075,000 | $2,050,000 |
| B | $3,300,000 | $100,000 |  |  |  | $50,000 |  | ($25,000) | $1,425,000 | $625,000 | $2,050,000 |
| C | $3,200,000 | $100,000 | ($5,000) |  |  | $50,000 |  | ($10,000) | $1,335,000 | $735,000 | $2,070,000 |
| D | $3,000,000 | $100,000 |  |  |  | $50,000 |  | ($10,000) | $1,140,000 | $940,000 | $2,080,000 |
| E | $2,800,000 | $100,000 |  |  |  | $50,000 |  | ($1,000) | $949,000 | $1,149,000 | $2,098,000 |
| F | $2,150,000 | $100,000 |  |  |  | $50,000 |  |  | $300,000 | $1,800,000 | $2,100,000 |
| G | $2,900,000 | $100,000 |  |  |  | $50,000 |  |  | $1,050,000 | $1,050,000 | $2,100,000 |
| H | $2,900,000 | $100,000 |  |  |  | $50,000 |  |  | $1,050,000 | $1,050,000 | $2,100,000 |
| I | $3,750,000 | $100,000 |  |  |  | $50,000 |  | ($10,000) | $1,890,000 | $190,000 | $2,080,000 |
| J | $2,900,000 |  |  | $200,000 |  | $50,000 |  |  | $850,000 | $1,150,000 | $2,000,000 |

**A.7 Contract Negotiation Performance Results: Displayed to Class**

Results when no pre-quiz required

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Team | Price | Profit for Seller | Profit for Buyer | Joint Profits |
| A | $2,900,000 | $1,010,000 | $1,010,000 | $2,020,000 |
| B | $2,900,000 | $1,026,500 | $1,026,500 | $2,053,000 |
| C | $2,500,000 | $640,000 | $1,440,000 | $2,080,000 |
| D | $2,900,000 | $1,039,000 | $1,039,000 | $2,078,000 |
| E | $7,400,000 | $5,320,000 | ($3,380,000) | $1,940,000 |
| F | $4,000,000 | $1,925,000 | $25,000 | $1,950,000 |
| G | $2,900,000 | $789,000 | $1,089,000 | $1,878,000 |
| H | $2,900,000 | $1,010,000 | $1,010,000 | $2,020,000 |
| I | $2,900,000 | $815,000 | $1,115,000 | $1,930,000 |
| J | $2,900,000 | $830,000 | $1,130,000 | $1,960,000 |
| K | $3,000,000 | $1,145,000 | $945,000 | $2,090,000 |
| L | $2,900,000 | $835,000 | $1,135,000 | $1,970,000 |
| M | $2,900,000 | $1,020,000 | $1,020,000 | $2,040,000 |
| N | $2,250,000 | $399,000 | $1,699,000 | $2,098,000 |
| O | $3,000,000 | $1,104,500 | $904,500 | $2,009,000 |
| P | $2,900,000 | $1,049,000 | $1,049,000 | $2,098,000 |

Results when Pre-quiz required

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Team | Price | Profit for Seller | Profit for Buyer | Joint Profits |
| A | $2,850,000 | $975,000 | $1,075,000 | $2,050,000 |
| B | $3,300,000 | $1,425,000 | $625,000 | $2,050,000 |
| C | $3,200,000 | $1,335,000 | $735,000 | $2,070,000 |
| D | $3,000,000 | $1,140,000 | $940,000 | $2,080,000 |
| E | $2,800,000 | $949,000 | $1,149,000 | $2,098,000 |
| F | $2,150,000 | $300,000 | $1,800,000 | $2,100,000 |
| G | $2,900,000 | $1,050,000 | $1,050,000 | $2,100,000 |
| H | $2,900,000 | $1,050,000 | $1,050,000 | $2,100,000 |
| I | $3,750,000 | $1,890,000 | $190,000 | $2,080,000 |
| J | $2,900,000 | $850,000 | $1,150,000 | $2,000,000 |

# **APPENDIX B: Contract Management Exercise**

**Company Profile: Ace 1 Corporation**

Ace 1 is a New York corporation that manufactures high-end lighting fixtures (table lamps, chandeliers, and similar products). The company’s major customers are custom home builders and residential high-rise developers across the United States. Architects and designers often specify Ace 1 products when they are seeking stylish and high-quality lighting to achieve a coordinated look throughout a project. Ace 1 proudly advertises that its products are made in the United States.

Ace 1 products have been traditional electrical fixtures, operated by a switch or dimmer. There is an increasing demand for lighting that works with various smart-home technologies. The company recently lost out on a big contract because it doesn’t offer that feature. Ace 1 is seeking a vendor that can provide electronic modules that can be installed within the parameters of its existing designs

Ace 1 has a reputation for quality, but an event last year threated the company’s good will. A small fire broke out during a Custom Home Tour. No one was injured, but the real estate agent at the house tweeted a picture of the fire and blamed it on an Ace 1 lamp. The agent deleted the tweet after the Ace 1 CEO asked her to do so, but it had already been seen and commented on by several customers. Ace 1 tested the lamp and determined that there was indeed a wiring issue that caused the fire. Ace 1 did not release this information, but did pay for the repairs to the house. The company is also facing increased competition, so it is important that the products have top quality finishes and parts.

Ace 1’s head of manufacturing recently met with a rep from Component World, a company headquartered in California. The rep says that CW can deliver smart-home modules that will fit Ace 1’s designs. Ace 1 wants to close this contract quickly and start offering new versions of the designs before the next building season. The draft contract for this deal was written by the Component World rep; it is attached as Contract 1.

Meanwhile, the president of Component World heard about the potential deal and looked up Ace 1’s website. Component World is sponsoring a show home in California, and wants to buy all the fixtures—with CW modules—for the show home. Ace 1’s attorney put together a contract for that transaction. The draft contract is attached as Contract 2.

**Company Profile: Component World, Inc.**

Component World is a California corporation that sells electronic components. CW manufactures some of the units at its Fresno-area facility, but imports others from a manufacturer in China that works to CW’s specifications. CW does spot inspections on the imported units, and has never identified a quality control problem. Sometimes the Chinese supplier does not ship on time, and that leads to inventory problems. CW will buy replacements from other suppliers if the imports are late and domestic production is running behind. The company usually doesn’t have time to check these units; if there is a problem, CW just replaces the faulty unit when inventory is restored. A failed unit defaults to “off,” and is not a fire risk. Recently, CW started requiring buyers to inspect the units themselves, and disclaims problems that aren’t reported shortly after delivery. If such a buyer has a unit fail, then they must buy a replacement; they aren’t a lot of money individually. The CEO also believes that adding this term to the contract will reduce the possibility of lawsuits. The CEO formerly led a company that was sued many times, and has made lawsuit avoidance a priority at CW.

Component World has sales representatives operating around the country. The rep for New York state just met with an executive from Ace 1, a New York company that makes light fixtures. Ace 1 wants a particular unit that it can use to integrate lighting fixtures into smart-home and security systems. The rep says that the size of the unit is very important to Ace 1 because the company does not want to change its existing fixture molds. The units need to fit inside the fixtures. The specs for the unit are a millimeter under the maximum size that Ace 1 mentioned, which is tight, but it should work if all the units are consistent. The rep shared a sample with Ace 1 that fit in the required space.

Each unit sells for $7.97 in quantities over 10,000. Ace 1 wants 25,000, but it wants them fast and Component World doesn’t have enough on hand to fulfill the order immediately. The sales director recommends that the rep promise delivery within three months, and allow for partial shipments just in case there is a problem getting the product ready (or in case it needs to be brought in from the factory in China). The director also recommends making no special promises about unit size. The draft contract that the CW rep put together for this deal is attached as Contract 1.

Component World’s president is working on some marketing projects. CW will sponsor a show home in a local tour this year. The president already knew about Ace 1 lighting, and is interested in both landing the supply deal (Contract 1) and in having Ace 1 provide the most stylish and current lights for the show home. It is essential that the lights be delivered in perfect condition to the construction site by the date that the electrician will install them. The president spoke with an executive at Ace 1 about the idea, and then the Ace 1 attorney drafted a contract for the parties to review. That agreement is attached as Contract 2.

**Contract 1**

**Sale of Goods Contract**

WHEREAS Ace 1 Corp. (“BUYER”) wishes to buy electronic components (“GOODS”), AND

WHEREAS Component World, Inc. (“SELLER”) is in the business of selling electrical components, AND

WHEREAS SELLER wishes to sell GOODS to BUYER,

NOW THEREFOR SELLER and BUYER (the “PARTIES”) enter into this agreement (“AGREEMENT”) effective as of the last date given below.

1. SALE: SELLER agrees to transfer ownership and rights to GOODS to BUYER for the agreed-upon compensation (“PURCHASE PRICE”). SELLER warrants that SELLER has full right and authority to so transfer GOODS.
2. PURCHASE PRICE: BUYER agrees to pay SELLER $199,250 (ONE HUNDRED NINETY-NINE THOUSAND TWO HUNDRED AND FIFTY U.S. DOLLARS) upon satisfactory receipt of GOODS with accompanying invoice for the total amount of $199,250 (ONE HUNDRED NINETY-NINE THOUSAND TWO HUNDRED AND FIFTY U.S. DOLLARS).
3. DELIVERY: SELLER will provide GOODS to BUYER by shipping to BUYER’S facility using SELLER’S preferred trucking company. All GOODS will be adequately packaged to avoid damage (packaging included). BUYER will pay trucking costs on receipt of trucking invoice forwarded by SELLER.
4. GOODS: The GOODS will consist of the component discussed by the PARTIES, and the shipment(s) will include 5,500 individual components of that type. Each component will be exactly as shown in SELLER samples/catalog for that component.
5. SHIPMENT: SELLER will pack and ship GOODS in no more than two shipments, with the first shipment containing at least half of the contracted GOODS. All GOODS will be shipped within three months of the date of this contract.
6. DISPUTES: BUYER will inform SELLER of any problems with GOODS within 72 hours of receipt. SELLER is unable to accept returns for any reason after 72 hours. If timely notice is not received, BUYER will be considered to have unconditionally accepted GOODS.
7. MISCELLANEOUS: Beyond this contract, neither BUYER nor SELLER has made any statements that either PARTY is relying upon.

The PARTIES hereto agree to the foregoing as evidenced by their signatures inscribed below as of the last date given thereto.

ACE 1 CORP. COMPONENT WORLD, INC.

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ Date:\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ Date: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

**Contract 2**

**Supply Contract**

Effective Date: The latest date shown in the signature section below.

Parties: Ace 1 Corp, a New York corporation, SELLER

Component World, Inc., a California corporation, BUYER

Subject of Contract: Lighting fixtures and lamps for CW Show Home from the “Lightspace” product series, in specific quantities and types as set forth in the attached appendix [omitted], incorporated herein by reference.

Applicability: This contract summarizes the agreement of the SELLER and BUYER for purchase of the lighting products specified in the appendix. The products will be sold by the SELLER in accordance with and subject to the Terms and Conditions provided below.

Terms and Conditions:

1. Delivery: BUYER will arrange and pay shipping to the CW Show Home. SELLER will provide adequate packaging to prevent damage to goods of this sort and make packaged products available to BUYER’s shipper. Partial shipments are acceptable. All products will be made available to BUYER’s shipper at least four business days before the Show Home event. Timely delivery is of the essence. Title and risk of loss pass to BUYER upon pick-up by shipper.
2. Technician: SELLER will provide a technician employed by SELLER to travel to the CW Show Home to oversee installation and testing of the products shown in the appendix. If any light does not function properly in all aspects, the technician will remedy the issue within 24 hours. BUYER will bear all costs associated with the technician at 30% over actual cost.
3. Product Appearance: If any product has a visible flaw, BUYER will email an image of the issue. SELLER will ship a replacement part if the image shows a flaw larger than a half-inch square.
4. Labelling: SELLER will be credited in the Show Home catalog and in tent cards on-site. All credits will include “featuring Component World smart-home electronics” in the text. SELLER’s logo and name will be no less than 50% larger than BUYER’s name.
5. Production: SELLER may contract for production with the entity of its choice.
6. CW Components: SELLER warrants that all products provided under this agreement will contain CW “smart home” components. SELLER disclaims liability for any failure of or damage caused by the failure of these components.
7. Payment: The price is shown in the appendix. BUYER must remit payment in full prior to any of the goods being made available for shipment by SELLER.
8. Quality: With the exception of the CW components contained within the products, SELLER warrants that all products will be fit for their intended purpose upon shipment.
9. Indemnification: BUYER shall defend, indemnify, and hold harmless SELLER, its subsidiaries, affiliates, successors, or assigns against any and all loss, injury, death, damage, liability, claim, action, judgment, award, fine, cost, or expense, including reasonable attorney and professional fees and costs, up to and including the cost of enforcing said indemnification against BUYER, arising out of or occurring in connection with the products shown in the appendix.
10. Applicable Law: This agreement shall be governed by the law of the state of New York.
11. Disputes: Any disputes arising out of or in connection with this agreement will be submitted to the state trial court of New York. BUYER and the court shall waive any objection to jurisdiction over any such dispute.
12. Complete Agreement: This contract and its appendix form the sole and entire agreement of the BUYER and SELLER with respect to this transaction. As such, it supersedes any prior or contemporaneous understandings, negotiations, or other communications of any sort, whether written or oral, with regard to this transaction.
13. Signatures: The signatures below indicate the parties’ willingness to be bound by this agreement.

ACE 1 CORP. COMPONENT WORLD, INC.

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

Date: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ Date: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

**Sample Contract for Exercise Introduction**

Hand out or project this short contract and work with students to identify the contract’s object; parties; price and timeline; warranties; dispute resolution; and termination provisions.

Automobile Purchase Agreement

Date: March 30, 2019

Buyer Joey Jojoh (signature below) agrees to buy a 2005 Nissan Sentra, vehicle identification number 1NIS49275XT2396UY, from SUPER USED CARS OF HOOTERVILLE, INC. (Seller) for ONE THOUSAND ONE HUNDRED FIFTY DOLLARS ($1,150), plus applicable sales tax and license fee.

* Buyer affirms that Buyer has declined a $100 “safe-car” inspection by Seller. Seller therefore makes no representations regarding the safe condition or operation of the vehicle.
* Seller is making no promises that Buyer is relying on, other than (1) the vehicle contains a new battery installed on March 20, 2019, with adequate power to start the vehicle, should the vehicle be otherwise in working order, and (2) the SUPER SATISFACTION GUARANTEE detailed below.
* Payment due at pick-up at the SUPER USED CARS lot; pick-up to occur within two business days of the date given above.
* SUPER USED CARS retains the right to refuse payment and pick-up if Buyer does not bring identification or if Buyer is intoxicated.
* No trade-in agreed.
* Any disputes will be subject to final and binding arbitration through SUPER DISPUTE RESOLUTION, located across the street from SUPER USED CARS. Buyer must inform SUPER USED CARS and SUPER DISPUTE RESOLUTION of any claims by registered letter.
* Buyer and Seller agree that no disputes will be brought after conclusion of the SUPER SATISFACTION GUARANTEE period plus two business days.

SUPER USED CARS SUPER SATISFACTION GUARANTEE! If the vehicle breaks down through no fault of the buyer within three days of purchase and the vehicle is determined by SUPER USED CARS to be unrepairable for less than 150% of the amount paid for the vehicle, SUPER USED CARS will refund the buyer, less a 5% restocking charge for return of the vehicle.

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

Joey Jojoh

**Group Worksheet**

1. Identify at least two provisions in each contract that you would want to change to better serve your company’s interests or the interests of both parties. Briefly explain why you selected these items.

Contract 1







Contract 2




2. Name at least one important missing contract provision that your company would want to include in each contract. Explain why you chose that provision in terms of your company’s interests.
3. (Optional) Select either contract and identify at least one important provision that is currently missing that the *other* company would want. Explain why you chose that provision.

**Rubric for Single-Session Version (Group Grading)**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Component** | **Excellent** | **Very Good** | **Satisfactory** | **No Points** |
| Identifies problematic clauses in both contracts | Accurately identifies major problematic clauses in both clauses | Identifies some problematic clauses; may identify some minor issues | Identifies few problematic clauses; may prioritize minor issues over major clause problems | Does not identify major problematic clauses |
| Explains how each identified clause is problematic for the parties | Clearly explains how each identified clause may cause problems | Accurately explains how some clauses may cause problems | Offers incomplete or partially inaccurate explanations | Fails to link identified clauses with potential problems |
| Identifies missing clauses the assigned company would want | Accurately identifies at least one missing clause for each contract that the assigned company would want | Identifies at least one clause that should be included in one of the contracts for the assigned company | Identifies missing clause that the opposite party would want, or identifies minor missing clause | Fails to identify important missing clauses |

1. *See* <http://computer.howstuffworks.com/dell-battery-fire.htm>. [↑](#footnote-ref-1)
2. *See* <http://www.cpsc.gov/cpscpub/prerel/prhtml09/09221.html>. [↑](#footnote-ref-2)
3. *See* <http://support.apple.com/kb/TS2099>. *See* also <http://www.theregister.co.uk/2009/07/10/saab_inferno/> for a story where an iPod might have led to a fire that “torched” a Saab; <http://www.theregister.co.uk/2007/10/08/ipod_nano_blaze_horror/> for a story where an iPod might have caught someone’s pants on fire; and <http://www.meti.go.jp/english/press/data/nBackIssue20080819_02.html> for a story where an iPod’s “battery overheated and partially scorched a tatami mat.” [↑](#footnote-ref-3)
4. *See* http://computer.howstuffworks.com/dell-battery-fire.htm. [↑](#footnote-ref-4)
5. *See* <http://computer.howstuffworks.com/dell-battery-fire.htm>.

   [↑](#footnote-ref-5)
6. *See* <http://www.cpsc.gov/cpscpub/prerel/prhtml09/09221.html>. [↑](#footnote-ref-6)
7. *See* <http://support.apple.com/kb/TS2099>. *See* also <http://www.theregister.co.uk/2009/07/10/saab_inferno/> for a story where an iPod might have led to a fire that “torched” a Saab; <http://www.theregister.co.uk/2007/10/08/ipod_nano_blaze_horror/> for a story where an iPod might have caught someone’s pants on fire; and <http://www.meti.go.jp/english/press/data/nBackIssue20080819_02.html> for a story where an iPod’s “battery overheated and partially scorched a tatami mat.” [↑](#footnote-ref-7)
8. *See* http://computer.howstuffworks.com/dell-battery-fire.htm. [↑](#footnote-ref-8)
9. All damages will be shown to be the result of manufacturing defects. Manufacturing costs include any fees associated with importing and exporting. [↑](#footnote-ref-9)