



**Tips for Terminating a Long-Term Customer/Supplier Relationship**

Fees & Burgess, P.C.,  
Emphasizes:

From time to time, customers and their long-term suppliers end up parting ways for one reason or another. In the current economy, one possible reason might be a lack of confidence in the customer’s ability to pay, or questions as to the supplier’s continued solvency. Regardless of the underlying basis for the decision to end things, there is always a risk that the decision might trigger a lawsuit. Here are a few suggestions as to how you can prepare for this possibility in advance and make sure that you are in a good position if things go south.

Decide Things on the Front End

One of the most important steps that you can take to protect your company in these kinds of situations is to make sure that you have a solid written contract in place with all of your major suppliers/customers. All too often, suppliers and their customers choose to do business on nothing more than one, or both, of the parties’ boilerplate purchase/sales order terms and conditions. Granted, when it comes to individual transactions it is usually quite an accomplishment if you can get the party on the other side of the table to accept your standard terms, chances are that even your standard terms do not cover all of the significant legal issues that can come up in a long-term relationship. For example, how will residual inventory held by the supplier be handled? How will the parties deal with capital equipment and intellectual property in the supplier’s possession that is actually owned by the customer? How long will each party have to submit claims to the other for any outstanding obligations? Is this a situation in which one party may need to retain the right to use the other’s intellectual property for some period after the relationship terminates? If the customer is flowing through the supplier’s product warranties to its customers, how will warranty claims be handled after the supplier and the customer are no longer doing business? While the topics that should be covered in a company’s supply agreements will vary from industry to industry and from contracting party to contracting party, here are some basic principles that should be spelled out at a minimum:

- (1) **When is the right to terminate triggered?** Does it only apply if the contract is breached, or can one or both parties terminate for their convenience?

**General Civil Litigation**

**Commercial Law & Litigation**

**Municipal Law & Litigation**

**Police Civil Liability Defense**

**Employment Law & Litigation**

**Construction Litigation**

**Corporate Law & Government Contracting**

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**Corporate Counsel Services**



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- (2) **What kind of notice is required prior to termination?** Written notice is highly recommended, as is specifying how many days in advance the notice must be given prior to the termination becoming effective. On the customer's end, this notice period needs to be long enough to ensure that an alternate source can be located for the goods or services provided by the supplier.
- (3) **What are the potential areas of liability/exposure that termination will create for one or both parties?** If there are significant liabilities that are likely, or certain, to arise should the parties' relationship be terminated suddenly, those liabilities need to be called out and a procedure needs to be described for minimizing those liabilities. A good example is the residual inventory scenario mentioned above. If the supplier will probably have some parts, materials, finished goods, and/or work-in-process on hand at the time of termination, the contract should specify the circumstances under which the customer will purchase those items from the supplier, if any. Of particular concern should be whether the termination of the parties' relationship will impact third parties (e.g., subcontractors, second-tier suppliers, the customer's customer, etc.), as this is an area that could create liability for both parties.
- (4) **How long will the parties have to present their termination claims?** In order to promote some sense of finality, it is usually a good idea to have a deadline as to when each party must submit its claims to the other for compensation related to the termination. It is also best to have a time limit on how long a party can take to respond to a claim.

Clients frequently complain that trying to get a broad supply agreement in place with a customer or a vendor is a time-consuming process that risks scaring off the other party. If that is your concern, then at least see if you can get the other party to agree to a short-form agreement that will only govern major areas of concern, including termination issues, and will apply to all transactions between the parties. In many cases it is better to irritate or inconvenience the other party a little on the front end to avoid getting tangled up in a major lawsuit on the back end.



## **Tips for Terminating a Long-Term Customer/Supplier Relationship** *(continued from page 2)*

### Document, Document, Document

Another major step that companies can take to minimize their potential exposure when a customer-supplier relationship falls apart is to make sure they have sound document retention policies in place. The key here is taking the time to think through which documents you actually need to keep, and how you will organize them to make sure they can be recovered and searched quickly if you do end up in a lawsuit.

You should keep detailed records on any major change in how the parties do business. If a change is initiated over the phone or in person, it is probably smart to send a follow-up e-mail or letter describing the change and requesting a confirmation from the other party in writing that your understanding of the new practice is accurate. A lot of times, disputes that arise in connection with a termination relate to differences between what was in the parties' contract and how they actually did business. Some deviation from the contract is almost certain to take place in a long-term relationship, but you need to make sure that when it does occur there is some written record of that change. If you intend for the deviation to be a one-time occurrence, you need to put the other party on notice of that fact in writing before the change is implemented.

### Giving Notice

If your company is the one giving notice of its intent to terminate the relationship, there are some steps that you can take to try and reduce the chances of the other party running straight to their lawyer. The first is analyze your position in advance. Before you send notice, sit down with your contract, and make sure you know each party's rights and obligations with respect to termination generally, and notice of termination specifically. If you are terminating a contractual relationship based on a breach or anticipated breach, gather up all of the supporting documentation you can find to bolster your argument. By that same token, if you believe that your company will be entitled to recover certain expenses in connection with the termination of the relationship, pull together documentation supporting your claim.

When you do provide the other party with notice that you are terminating the relationship, try to be objective and professional, rather than accusatory and argumentative. Be sure that you provide the other party with any appropriate documentation supporting your right to terminate and any claims you may have in connection with the termination. It is a good idea to reference any contract provisions that support your position. If you present your notice in a way that shows you have done your homework and that your decision to terminate was not based on some personal grudge, you make it less likely for the other party to want to spend the time and money to challenge you.

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## **Proposed Changes to Rules for Determining Country of Origin for Imported Merchandise**

U.S. Customs and Border Protection (CBP) issued a Notice of Proposed Rulemaking on July 25, 2008, stating its intention to amend the existing rules for determining the country of origin for imported goods. In the majority of cases, the current system, which has been in place for almost one hundred years, uses the subjective “substantial transformation” test to determine country of origin. CBP proposes abandoning this approach in favor of using the “tariff shift” test found in 19 Code of Federal Regulations Part 102, which currently applies to trade between North American Free Trade Agreement countries. Under the proposed rule, the “tariff shift” test would be applied across the board, with some limited exceptions. The goal behind the change is to increase predictability and objectivity in making country of origin determinations.

While the “tariff shift” test can, in some instances, allow for speedy determinations of a product’s country of origin, it is a complex test to apply that in many cases will require more time and mental effort to make a determination. The test specifies that the country of origin for an imported good is the country where: (1) the good is wholly obtained or produced; (2) the good is produced exclusively from domestic materials; or (3) each foreign material incorporated in the good undergoes an applicable change in tariff classification. This third option is what is meant by a “tariff shift,” and the process for determining when this has occurred is often far from simple.

If implemented, compliance with this rule would require companies to review and rework their existing policies and procedures for making country of origin determinations, and may necessitate their hiring additional personnel to handle the complex analysis that will be involved in making these determinations. In addition, some companies may find that goods that were compliant with the Trade Agreements Act of 1979 under the old framework are not complaint under the “tariff shift” test. So, if this rule does go into effect, companies might be wise to go back and reevaluate their country of origin determinations as to some of the goods they routinely import to see if using the “tariff shift” test will change their previous determinations.

The comment period for this proposed rule expired on December 1, 2008, but a final rule has yet to be issued.

The Notice of Proposed Rulemaking can be found at:  
73 Fed. Reg. 43,385 (July 25, 2008)  
<http://edocket.access.gpo.gov/2008/pdf/E8-17025.pdf>



## **New Government Policy Favoring Project Labor Agreements on Major Federal Construction Projects**

On February 6, 2009, President Obama signed Executive Order 13502 putting into place a new government policy encouraging federal agencies to require the use of project labor agreements (PLAs) on federal construction projects that carry a price tag of \$25 million or more when it is consistent with the law to do so, and having such an agreement in place will advance the government's interest in achieving economy and efficiency in federal procurement, produce labor-management stability, and help ensure compliance with laws and regulations governing workers' rights. The order defines a PLA as "a pre-hire collective bargaining agreement with one or more labor organizations that establishes the terms and conditions of employment for a specific construction project." "Labor organization" basically means a labor union. This order expressly revokes Executive Orders 13202 and 13208, which were signed by President Bush and prohibited agencies from requiring contractors to enter into PLAs as a condition to being awarded a federal construction contract.

The order specifies certain contract terms that must be included in any PLA that is entered into on one of these major federal construction projects. These terms are aimed at binding all contractors and subcontractors involved in the project to the PLA, and making sure there is a procedure in place to resolve any labor-management disputes. The mandatory terms would also prohibit any strikes, lockouts, or similar activities.

The order does not require executive agencies to use PLAs, or restrict the circumstances in which they can require them. It also does not require contractors or subcontractors to enter into a PLA with any particular labor organization, and it does not give preferential treatment to contractors or subcontractors who have collective bargaining agreements with unions outside of the specific construction project at issue. While this policy may not discriminate against non-union shops in awarding construction projects, it could result in more of these shops having to subject their workforce to union involvement on a project-specific basis.

President Obama's order gives the Federal Acquisition Regulatory Council 120 days to amend the Federal Acquisition Regulation to implement these changes. It also directs the Office of Management and Budget, the Secretary of Labor, and other officials to provide President Obama with recommendations within 180 days as to whether broader use of PLAs, with respect to construction projects undertaken by the federal government or projects receiving federal aid, would help promote the economic, efficient, and timely completion of such projects.

Executive Order 13502 can be viewed at: [http://www.whitehouse.gov/the\\_press\\_office/ExecutiveOrderUseofProjectLaborAgreementsforFederalConstructionProjects/](http://www.whitehouse.gov/the_press_office/ExecutiveOrderUseofProjectLaborAgreementsforFederalConstructionProjects/)



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*HR Update*, presented to the Huntsville chapter of Associated Builders and Contractors

June 10, 2009—Decatur, AL

*Conducting Effective Investigations in the Workplace*, presented to the Decatur chapter of Society for Human Resource Management

June 11, 2009 – National Contract Management Association Audio Seminar Series

*Uniform Commercial Code*

June 12, 2009 – Boston, Massachusetts

*Contract Management and Business Arrangements: Risk Allocation in Critical Areas of the Contract*, presented as part of *EMS Training II:Part C of the IPC EMS program Manager Training and Certification Program*

September 9, 2009 – Birmingham, Alabama

*Wage & Hour Master Class*, presented for, and sponsored by, M. Lee Smith Publishing, Inc.

September 24-25, 2009 – Chicago, Illinois

*Contract Management and Business Arrangements: Risk Allocation in Critical Areas of the Contract*, presented as part of *EMS Training II:Part C of the IPC EMS program Manager Training and Certification Program*



If you would like more information on these seminars, please go to [www.feesburgess.com](http://www.feesburgess.com)





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