

**COMPONENT MANUFACTURERS—
SUCCESSFULLY NEGOTIATING AN ACCEPTABLE
CUSTOMER CONTRACT—THE FIRST STEPS**

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Pagel, Davis & Hill, P.C. (the “Firm”) is a Houston based law firm with a diversified practice that includes a focus on providing the services required for many companies serving the construction industry. Mr. Pagel, the President and Senior Shareholder of the Firm, serves as outside general counsel to WTCA – Representing the Structural Building Components Industry.

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About the Presenter

As the president and a senior shareholder of the Houston, Texas law firm of Pagel, Davis & Hill, a professional corporation, Kent J. Pagel's practice involves the local, regional, and national representation of companies in construction contracts, risk management techniques and litigation, insurance and product liability matters.

Mr. Pagel's clients include wall, truss and component manufacturers and other numerous segments of the construction industry--including owners, general contractors, subcontractors and other trade suppliers. Mr. Pagel and his firm also serve as outside general counsel for *WTCA—Representing the Structural Components Industry* and the *Engineered Wood Products Association*. Mr. Pagel is furthermore a regular writer and lecturer on liability (including construction defect litigation), risk management, and insurance issues facing companies in the construction industry. Mr. Pagel writes frequently for *Structural Building Components Magazine*.

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What do we mean by “Customer Contracts” and Initial Recommendations

- What do we mean by **customer contracts**?
 - Those contracts entered into verbally or in writing by component manufacturers
 - When products or services are being sold to their builder and general contractor customers.
- Customer contracts play a big part in the degree of risks and liabilities assumed by component manufacturers.
- INITIAL RECOMMENDATIONS:
 - Customer contracts should be in writing.
 - Recommended starting point—component manufacturer issues a written **bid** or **proposal** each time products or services are offered for sale.
 - Each bid should be submitted with written **terms and conditions of sale**.
 - If signed by the customer, the bid then becomes a written and enforceable customer contract.
 - HOWEVER—Even if the component manufacturer’s bid is fair, customers may request or even insist on the manufacturer signing the customer’s written contract form.

The Builder's Customer Contract Form

- Builders and contractors demand their customer contract forms be signed--BECAUSE
 - They have been reviewed by their attorneys and risk managers
 - Time and money is saved and risk may be avoided by not having to review suppliers' forms
 - They are truly one-sided

- Customer contract forms from builders and general contractors go by many different names—HOWEVER IT IS NOT THE NAME BUT THE CONTENT THAT MATTERS!
 - Subcontract Agreement
 - Material Supplier Agreement
 - Vendor Agreement
 - Construction Agreement
 - Purchase Order

- Our focus and goal:
 - What provisions are most problematic and why.
 - Seek a contract that fairly allocates all risks.

The Component Manufacturer's Mindset

- What is the Component Manufacturer's mindset?
 - “We sign anything”
 - “We need this customer to survive”
 - “We negotiate every paragraph”
 - “We take the middle course by negotiating the more problematic provisions.”

- We recommend a focus on primarily dealing with problematic provisions—some may refer to these as potential DEAL KILLERS.

- Examples of important provisions to the component manufacturer—do any amount to DEAL KILLERS for your company?
 - Payment terms
 - Pricing provisions
 - Scope of work provisions
 - Warranty provisions
 - Risk Transfer, including indemnity and insurance requirement provisions
 - Scheduling and delivery provisions
 - Default and termination provisions

How to Effectively Review the Customer Contract Form

- Develop formal or at least informal internal procedures.
- All customer contract forms are not the same.
- Identify the more problematic provisions.
- Example of a review of payment provisions contained in a builder's form material supplier agreement:
 - Purchase price
 - Payment terms
 - Retainage
 - Conditional payment provisions
 - Prompt payment discounts
 - Bond requirements

Customer Contract Negotiation Process

- Secure full and complete contract form as early as possible.
- Consider requesting a different contract form if a subcontract agreement form is presented.
- Consider beginning contract negotiation even before bidding.
- Know the builder's mindset—
 - Take it or leave it
 - “We do not permit any changes to our form”
- Negotiate—ALWAYS!

Negotiation Fundamentals

- Selling the customer on fairness—e.g. defending the builder for its negligence as compared to defending the builder from your negligence.
- Emphasize that a component manufacturer who does not care about the risks contained within a customer contract form may not care about the quality of design or manufacturing.
- Negotiation is an art and not a science.
- One negotiation is all it may take.
- Must I use a lawyer to negotiate?
- How can my insurance broker help?
- Do not wait to the last minute to negotiate.

Means to Negotiate

- Incorporating bid or proposal and terms and conditions of sale into the customer contract—at times this may work.
- Use of strikethroughs and additions to the face of the customer's form contract.
- Use of a letter:

Dear Mr. _____:

We have reviewed your proposed Agreement and can accept same subject to the following clarifications. I would request that you either sign below acknowledging your acceptance of such conditions or set forth these changes in a revised version of the Agreement.....

- Use of Customer Contract Addendum Form:

The undersigned Supplier accepts the terms of the proposed Agreement subject to the Contractor's acceptance of this addendum. The Contractor may signify his acceptance by signing this addendum, or by permitting Supplier to begin work.....

- Use of the Additions and Deletions approach:

Supplier accepts the terms of the proposed Agreement subject to Contractor's acceptance of these Additions and Deletions to the Agreement which shall modify the terms of the Agreement. Contractor shall signify its acceptance by either signing below or including these Additions and Deletions in a re-draft of the Agreement.....

- Make sure it gets signed.

Here we go...

- We will review and explain sample language from a builder's customer contract form.
- With each sample provision we will assign a risk rating using an A to F grading scale, with pluses and minuses similar to what most of us have experienced in school. Our focus will be on the following types of provisions with one or more modules assigned to each type of provision.
 - Payment
 - Pricing
 - Scope of work and design responsibilities
 - Indemnity
 - Insurance requirements
 - Warranty
 - Scheduling and delivery, and
 - Default and termination
- For each type of sample provision that we examine we will offer up one or more alternative provisions and we will further assign a risk rating to each alternative provision.
- As to our risk rating system, it is important to note that this system is very subjective. It is also important to know that there are no solid lines when moving from one risk rating to another.
- For example moving from a risk rating of A to F clearly means the contract provision rated A is highly favorable to the component manufacturer as compared to the contract provision rated F which is very adverse in terms of risk to the manufacturer. However, comparing a provision with risk rating of B to one with a rating of C—while we believe the provision rated C presents greater risk to the manufacturer, there are no measurable ways to describe why we rate particular provisions differently—thus the ratings are not objective.
- Terms we will use include: Supplier, Contractor, Owner, Agreement, and Work.

SAMPLE CUSTOMER CONTRACT PROVISIONS—Payment Provisions

[Sample Customer Contract Provisions]

Contractor agrees to pay Supplier the sum of \$100,000.00 (the “Purchase Price”). The Purchase Price shall be payable within 10 days of receipt of payment from Contractor by Owner. Supplier represents and acknowledges that it relies primarily on the credit and ability of the Owner and not Contractor, and Supplier agrees that payment by the Owner to the Contractor, shall be an express condition precedent to any payment obligation that Contractor may have to Supplier.

COMMENT: Be aware of “condition precedent language”.

Ten percent (10%) of each of Supplier’s invoice amounts shall be withheld as retention and shall be held in total, as accumulated, to be reduced when and to the extent the Contractor in its sole discretion deems proper.

COMMENT: Do you accept retainage?

Supplier hereby waives and releases all liens or rights of liens now existing or that may hereafter arise for any and all work or labor performed or material furnished under this Agreement.

COMMENT: Do you know the difference between a waiver of lien provision and a partial or final lien waiver?

Upon Contractor’s request as determined in its sole discretion, Supplier shall pay for and furnish to Contractor, a good, sufficient and acceptable 100% Performance Bond and a 100% Payment Bond on Contractor’s standard bond forms, written by a surety company acceptable to Contractor. The cost of the bonds required herein is included in the Purchase Price.

COMMENT: Do you know what these bonds accomplish; can you provide such a bond?

RISK RATING: F

COMPARE:

[Sample Alternative Provision]

Contractor agrees to pay Supplier the Purchase Price at the times and in the manner hereinafter set forth. No contract retainage shall be permitted. Payment by Owner shall not be a condition precedent of payment by the Contractor to Supplier. Supplier shall release its liens only to the extent of payments received. Supplier’s requirement to provide a performance or payment bond is deleted in its entirety.

COMMENT: This provision eliminates: retainage; the pay-if-paid provision; waiver of lien rights; and bond requirement provision.

RISK RATING: A

SAMPLE CUSTOMER CONTRACT PROVISIONS—Pricing Provisions

[Sample Customer Contract Provision]

Supplier's prices shall be fixed for the duration of the project. Supplier further represents that the Purchase Price charged is the lowest price charged by Supplier to buyers of a class similar to Contractor under conditions similar to those specified in this Agreement.

COMMENTS: What are the risks of fixing pricing for the duration of the project? Do you understand the risks of “most favored pricing” provisions?

RISK RATING: F

COMPARE:

[Sample Alternative Provision]

In the event of a price increase, all unfilled orders manufactured and shipped after a date set out in the approved delivery schedule will be invoiced at the increased price unless cancelled by Contractor by notice received by the Supplier before manufacturing and shipment.

Delete the provision in the Agreement that Supplier's prices are the lowest prices charged to buyers of a similar class to Contractor as such provisions are not applicable to the truss and component industry given the unique shapes and sizes of the products manufactured.

RISK RATING: A

SAMPLE CUSTOMER CONTRACT PROVISIONS—Scope of Work Provisions

[Sample Customer Contract Provisions]

Supplier shall assume all obligations existing under the Contract Documents which consist of: (a) this Agreement, including any exhibits or attachments; (b) the General Contract between the Contractor and Owner; and (c) the drawings, plans, and specifications.

COMMENT: Be aware of “flow-through” or “flow-down” provisions.

Supplier shall furnish and deliver all requirements of wood floor and roof trusses, including but not limited to: (1) engineered floor and roof trusses per plans and specifications; (2) sealed engineering; (3) all bracing; (4) all truss to beam and truss to truss connectors per Supplier design; (5) all other truss system requirements; (6) shop drawings per lead time of not more than 7 days; (7) field measuring; and (8) all required repair details.

COMMENTS: How bad can it get?

All truss designs shall require a species and grade of truss lumber at a minimum grade of #2 kiln dried Southern Pine or Western Lumber.

Trusses shall be fabricated in accordance with a building code approved third party inspected quality control program.

Supplier shall indicate all lateral and point loads generated by truss systems and all specific requirements for installed permanent bracing. Trusses to be marked to match erection plans provided to Construction Manager.

Upon Contractor's request, Supplier shall inspect completed installation with all permanent bracing installed and issue an engineering letter of approval noting approval and/or deficiencies observed.

COMMENT: Are you insured for this risk?

RISK RATING: F

COMPARE:

[Sample Alternative Provision]

Supplier will provide those products described on its bid which is attached and no other products shall be provided.

COMMENT: Quantify and qualify as to the products you are furnishing ARE NOT furnishing.

Supplier shall comply with those Contract Documents provided by Contractor, including any project specifications, only as agreed to by Supplier.

Supplier shall submit for review and approval: (a) truss design drawings; and (b) a truss placement plan which will indicate the location of the trusses assumed by Supplier based on Supplier's review of the plans provided. The truss design drawings shall be signed and sealed by a licensed engineer. The truss placement plan shall not be signed and sealed.

COMMENT: The component manufacturer's standard truss drawings submittal.

Supplier shall depict on its truss design drawings the required permanent lateral web member bracing locations. Supplier shall have no responsibility to design the size, connections, and anchorage of the permanent continuous lateral web member bracing. The design or determination of all temporary and permanent bracing for the building's structural system shall be furnished by others.

Contractor and its installation subcontractors, and not Supplier, shall be responsible for: (a) inspecting the products for defects in quality after delivery; (b) handling and storing of the products; (c) field measuring and verifying the dimensions or adequacy of work done by other trades as it may affect the products; (d) installing, bracing (and bracing connections), and connections of the products to the supporting structure; and (e) inspecting the installation of the products. Handling, storage, installation and bracing guidelines in the form of BSCI summary sheets produced jointly by the Wood Truss Council of America and the Truss Plate Institute shall be provided by Supplier within its job-site package.

RISK RATING: A

SAMPLE CUSTOMER CONTRACT PROVISIONS—Indemnity Provisions

[Sample Customer Contract Provision]

COMMENT: Let's break this BEAST apart!

“To the fullest extent permitted by applicable law, the Supplier expressly agrees to defend (at Supplier's expense and with counsel acceptable to Contractor), indemnify, and save and hold harmless Contractor and all of its officers, directors...

COMMENT: This language identifies this as an indemnity provision and provides to whom the indemnity extends.

...from and against any and all claims, suits, losses, causes of action, damages, liabilities, and expenses of any kind whatsoever arising out of the performance or non-performance of the Work, including without limitation, all expenses of litigation..., arising on account of or in connection with injuries to or the death of any person whomsoever, or any and all damages to property (including the loss of use thereof)..., which injuries, death or damages arise from, or are in any manner connected with, the Work performed by or for the Supplier under this Agreement, or are caused in whole or part by reason of the acts or omissions or presence of the person or property of the Supplier or any of its employees, agents, representatives, Suppliers, or suppliers...

COMMENT: This language identifies the expenses and damages to which the indemnity will apply. The highlighted language identifies in part the scope of the indemnity provision.

...including without limitations, injuries, death or damages which arise from or in connection with, or are caused by, any act, error, omission or negligence of the Contractor or the Owner and all of their officers, directors, shareholders, employees, agents, material suppliers, or suppliers...

COMMENT: This language makes this a very broad indemnity provision—referred to as intermediate-form indemnity provision.

...except where such injuries or death are caused by the sole negligence of the Contractor.”

COMMENT: This language carves out the indemnity only slightly—without this language this would constitute a broad-form indemnity provision.

RISK RATING: D-

COMPARE:

[Sample Alternative Provision]

All provisions of indemnification set forth in the Agreement shall be modified to provide that Supplier's obligation to indemnify shall exist only upon a court or jury finding that the manufactured products supplied by Supplier are defective in their design or manufacture, or in the delivery of the Supplier's products to the Contractor's jobsite.

RISK RATING: A-

SAMPLE CUSTOMER CONTRACT PROVISIONS—Insurance Requirement Provisions

[Sample Customer Contract Provisions—our focus for this presentation excludes Workers Compensation and Automobile Liability insurance requirements which are fairly standard.]

Supplier agrees to carry and provide Contractor with an insurance certificate setting forth Commercial General Liability coverage of not less than:

Each Occurrence	\$1,000,000
Products/Completed Operations Aggregate	\$2,000,000
General Aggregate	\$2,000,000

The Commercial General Liability policy must include:

An Additional Insured Endorsement (equivalent to ISO form CG 20 10 11 85) naming Contractor as additional insured and shall be endorsed to be primary and non-contributory to any insurance which may be maintained by or on behalf of Supplier. In addition, Commercial General Liability Insurance Coverage, including additional insured coverage for Contractor, shall be maintained in force until expiration of the applicable statute of limitations for claims related to latent defects and construction improvements for real estate.

Supplier warrants that the design and engineering of its product is covered by Commercial General Liability insurance.

Supplier for itself and on behalf of its insurers, to the full extent permitted by law hereby waives and releases the Contractor and all additional insureds from liability to loss, damage or loss of property, at the project, which loss or damage is covered by such insurance, irrespective of the additional insured's negligence which may have contributed to or caused such loss, to the extent such damages are covered by Supplier's insurance or are required to be covered by the insurance requirements of Contractor.

The Commercial General Liability policy must include:

Supplier agrees to carry and provide Contractor with an insurance certificate setting forth Professional Liability insurance in the amount of \$1,000,000 for each occurrence.

Supplier further agrees to comply with the following insurance requirements:

- a) All policies must afford an unqualified thirty (30) days notice of cancellation to the additional insured(s) in the event of cancellation or non-renewal. The wording "Endeavor" and ... "but failure to mail such notice shall impose no obligation or liability of any kind upon the company" must be deleted from the certificate.
- b) All policies must be written by insurance companies whose rating in the most recent Best's Rating Guide, is not less than AVII.
- c) Supplier agrees to provide a full certified copy of any policy maintained by Supplier to Contractor upon Contractor's request.
- d) Nothing in this Exhibit shall reduce Supplier's obligations under this Contract. Supplier's procurement and/or maintenance of insurance shall not be construed as a limitation of liability or as full performance of the indemnification and hold harmless provisions of this Agreement.

RISK RATING: F

SAMPLE CUSTOMER CONTRACT PROVISIONS—Insurance Requirement Provisions [Continued]

COMPARE:

[Sample Alternative Provision]

Attached are certificates of insurance setting forth Supplier's insurance carriers and coverages in effect and Contractor acknowledges that at the time of execution of the Agreement such carriers and coverages are acceptable and comply with the terms of the Agreement and that no other insurance coverage is required.

COMMENT: One approach—“this is what I have and I want you to accept.”

Contractor and Supplier further agree: (a) Contractor will be named as additional insured only under Supplier's Commercial General Liability insurance policy and only as specifically stated in the sample certificate of insurance that is attached; (b) Supplier's obligation to provide insurance shall extend only through the last date of delivery of products; (c) that Supplier shall use best efforts to cause its Commercial General Liability insurance carrier to delete from the certificate the “endeavor to” and “failure to mail such notice shall impose no obligation or liability of any kind upon the company” language; (d) delete any requirement of Supplier to provide full and complete copies of insurance policies, either certified or uncertified; (e) delete the requirement that Supplier's commercial general liability insurance covers Supplier's design and engineering; and (f) delete the requirement that Supplier provide professional liability insurance.

COMMENT: More advanced approach—“this is what I have and let me further explain.”

RISK RATING: A

SAMPLE CUSTOMER CONTRACT PROVISIONS—Warranties

[Sample Customer Contract Provision]

Supplier warrants and represents to Contractor that the workmanship of the Work, including all materials to be provided by Supplier, and all other aspects regarding the Work shall be in conformance with this Agreement and be free from faults and defects of design, material and workmanship for a period equal to such time that Contractor is warranting the Project to the Owner. This warranty shall extend to all consequential damages resulting from such faults and/or defects of design, material and workmanship. The remedies provided in this warranty shall not limit or otherwise be restrictive but shall be cumulative and in addition to all other remedies of Contractor hereunder and under applicable state law, including all laws related to latent defects or fraud.

COMMENT: What materials are covered by the warranty? What is the scope of the warranty? What is the duration of the warranty? What remedies are available to the customer? Have implied warranties been effectively disclaimed?

RISK RATING: D

COMPARE:

[Sample Alternative Provision]

Supplier warrants for one year from date of delivery that its manufactured Products shall be new and of industry standard quality in the trade and within the description set forth in this Agreement. Any items not manufactured by Supplier are warranted only as warranted by the manufacturer of such items, otherwise all such items are sold on an “**AS IS**” basis. THE FOREGOING WARRANTIES ARE EXCLUSIVE, AND ARE IN LIEU OF ALL OTHER WARRANTIES (WHETHER WRITTEN, ORAL OR IMPLIED AND INCLUDING ANY REGARDING THE MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE) NOT SPECIFIED HEREIN, RESPECTING THIS CONTRACT. Supplier’s warranty shall exclude losses caused by improper or insufficient maintenance, normal wear and tear, and any improper operating, storing, handling, installation, and bracing. Supplier’s obligations and liabilities under this Contract are expressly and exclusively limited to repair or replacement of defective Products or, at the option of Supplier, to the refund of the purchase price. IN NO EVENT SHALL THE CONTRACTOR BE ENTITLED TO RECOVER FOR INCIDENTAL, CONSEQUENTIAL, OR SPECIAL DAMAGES, INCLUDING LOSS OF PROFITS, OR OTHER COMMERCIAL LOSS.

COMMENT: What materials are covered by the warranty? What is the scope of the warranty? What is the duration of the warranty? What remedies are available to the customer? Have implied warranties been effectively disclaimed?

RISK RATING: B+

SAMPLE CUSTOMER CONTRACT PROVISIONS—Schedule and Delivery Provisions

[Sample Customer Contract Provisions]

Contractor may schedule the Work of Supplier using any means appropriate in Contractor's sole discretion.

Title for all materials and work covered by estimates shall pass to the Contractor at such time that Contractor has accepted the materials or work.

COMMENT: Make sure schedules are agreed upon and title to the products passes at time of delivery! What about the possibility of damages occurring during delivery that are caused by jobsite conditions?

RISK RATING: C

COMPARE:

[Sample Alternative Provision]

All deliveries shall be made in accordance with a schedule approved in writing by an authorized representative of Supplier. Supplier shall furthermore be provided 2 weeks written notice of suggested delivery dates.

Absent Contractor agreeing to assume all responsibility for damages and expenses with respect to Supplier's tractors, trailers and cargo, Supplier's drivers reserve the right to not enter a jobsite for delivery if in the driver's reasonable opinion the jobsite is not suitable for safe and effective ingress and egress. Any damage occasioned by crossing of curbs, sidewalks, driveways, utility lines, etc. in connection with any delivery shall be the sole responsibility of Contractor.

Title for materials shall pass to Contractor at time of delivery.

RISK RATING: A

SAMPLE CUSTOMER CONTRACT PROVISIONS—Default and Termination Provisions

[Sample Customer Contract Provisions—or do we really need to review this as it most likely is not subject to negotiation]

Should the Supplier at any time refuse or neglect to supply material of proper quality, or refuse to follow plans and specifications, or fail to pay for materials for which it has received payment from the Contractor, or fail in any respect to prosecute the work on its part to be performed, the Contractor shall have the right to terminate the Supplier's right to proceed in whole or in part. In such event, the Supplier shall not be entitled to any further payments hereunder, whether due or not, and Contractor shall have the right to retain the entire Purchase Price, until the completion of the project. The Contractor may finish the Supplier's work by whatever method it may deem expedient and the Supplier shall be responsible to the Contractor for any cost occasioned thereby. Contractor shall be entitled to deduct all such costs from any and all funds withheld from the Supplier. In the event the costs of completion exceed the Purchase Price, the difference shall be immediately paid by Supplier to Contractor. In the event the Purchase Price exceeds the costs of completion, Supplier shall be paid the difference ninety (90) days following completion of the project.

The Contractor shall have the right to terminate this Agreement for convenience, for any reason whatsoever, by giving written notice of termination to Material Supplier. Such termination shall be effective upon receipt of notice by the Material Supplier. Termination for default, if wrongfully made, shall be effective upon receipt of notice by the Material Supplier. In the event of termination hereunder, the Material Supplier shall only be paid the actual price for Work in place. The Material Supplier shall not be entitled to damages, anticipated profits on unperformed portions of the Work.

COMMENT: They all essentially read the same. Focus on what is important.

RISK RATING: D

COMPARE:

In case of a good faith claim against Supplier for any defect or non-conformity with respect to the Products sold, written notice setting forth such defect or non-conformity must be submitted to Supplier within ____ days of the date of delivery. Supplier shall have no less than [insert number of days] business days from date of receipt of such notice to either accept such claim or commence any necessary repair or replacement of Product. The Contractor shall have no right to deduct the amount of any claim from Supplier's invoice without the prior written approval of Supplier.

Upon termination for convenience Supplier shall be paid for all products manufactured and delivered.

RISK RATING: B

The Online Risk and Liability Management Best Practices for the Structural Component Manufacturing Industry—ORisk

- ORisk is a comprehensive program intended to assist component manufacturers in identifying the liabilities - contractual and otherwise - they face and set forth recommended risk management and liability avoidance practices.
- Online program basics:
 - 4 **Training Paths** including (1) Customer Contracts; (2) Plant Best Practices; (3) Insurance Claims Handling and Litigation Management; and (4) Trucking Liability.
 - Each Training Path to contain three or more **Tracks**.

For example, the Customer Contract Training Path includes tracks for Bidding and Terms and Conditions of Sale; Negotiating Customer Contracts; Risk Transfer—Indemnity and Insurance Requirements Provisions; and Actual Negotiation of a Customer Contract.
 - Each Track contains as many as 25 **Modules**.
- Resources to enhance training experience:
 - A comprehensive **Glossary** of risk management and liability terms.
 - **Case Breaks**—providing case examples based on real-life situations faced by component manufacturers.
 - **Fast Fact/Best Practices** slides within certain modules identifying recommended best practices for component manufacturers in terms of risk management and liability avoidance.
 - **Printable Handouts** that are relevant to the educational training of particular modules.

And, to test your knowledge of the risk management and liability material presented, the subscribers will find a set of **ORisk Quiz Questions** at the end of each module. Questions will be in either a multiple choice or true/false format. After giving your answer, the correct answer and a **Quiz Answer Explanation** will appear.