

Annex AG – Specimen Agreement for Hardware

[Annex AG to Contract No 701578537]

Ministry of Defence

Commercial Exploitation of Defence Equipment Developed at Government Expense

[CEL Agreement No.]*

Delivery Team Details:

Interpretation etc.

1. In this Agreement the following shall have the effect with respect to interpretation:

- a. 'the Contract(s)' mean(s) Contract No(s)..... between the Ministry and the Contractor relating to / for ;
- b. 'Contract Article' means any article which uses the design produced under the Contract(s) and includes any sub-assemblies, components or spares thereof;
- c. 'Government-funded tooling' means jigs and tools, etc. provided or paid for by the Ministry and required for the production of a Contract Article;
- d. the 'Contractor' includes any subsidiary or associated company of the Contractor;
- e. 'leviable transaction' means a sale or any other transaction giving rise to levy under this Agreement;
- f. the 'Contractor's selling price' means, subject to the proviso hereto, the price for which the Contractor invoices its customer but excluding the cost of such of the following elements as are applicable and can be identified to the satisfaction of the Ministry:
 - (1) Freight costs and insurance.
 - (2) Cost of packing not developed at UK Government expense.
 - (3) The cost of ECGD servicing and other sales finance charges including interest on customer credit.
 - (4) The cost of any MOD inspection.
 - (5) Installation and commissioning costs where installation and commissioning form no part of the work under the development contract(s).
 - (6) Agents' fees and commission.

(7) The price paid by the Contractor for an article or articles supplied to them by a third party for incorporation in the Contract Article, but only if such third party has a separate commercial exploitation agreement with the Ministry relating to such article or articles and has been informed by the Contractor that such article or articles are being used for a leviabale transaction.

(8) Value Added Tax where applicable.

Provided that any element of profit which the contractor has included in the above items (1) - (8) shall not be so included.

g. 'Profit' other than for the purposes of the proviso to sub-clause f. of this Clause means the difference between the Contractor's selling price and the allowable costs prescribed by the Ministry for the purpose of the sale in question, provided such difference is a positive sum.

Sales and Licences

2. Should the Contractor sell any Contract Article, other than for any purpose set out in Clauses 5 and 6 hereof, the Contractor shall pay to the Ministry:

a. a levy for the use of the design to be calculated at [...] per cent of the Contractor's selling price [except that the percentage rate of levy may be revised at the end of the development contract if the Contractor or the Ministry can demonstrate that the design relied more, or less, on private venture research and development than was assumed in agreeing the levy rate]*.

b. a levy of **(Information Redacted)** per cent of the Contractor's selling price for the use of Government-funded tooling except that the rate of **(Information Redacted)** per cent shall be reduced appropriately where a substantial part of jigs and tools etc. used in connection with a sale or other transaction has not been provided or paid for by the Ministry;

except that, unless otherwise agreed by the Ministry, levy on individual sales above **(Information Redacted)** in value (for which purpose contemporaneous sales of the same equipment to the same customer will count as one sale) will be payable on an appropriate profit-sharing basis to be agreed between the Contractor and the Ministry before the contract of sale is entered into. The threshold of **(Information Redacted)** may be increased from time to time by the Ministry, in relation to future sales, to take account of inflation.

3. Should the Contractor grant a licence to manufacture Contract Articles, the Contractor shall pay to the Ministry a levy calculated at **(Information Redacted)** per cent of the gross receipts of the Contractor in money by way of royalties, licence fees or otherwise in respect thereof:

Provided that:

a. where the consideration consists wholly or in part of some benefit other than money the levy shall, in lieu of or in addition to such payments (as the case may be), consist of or include a sum representing **(Information Redacted)** per cent of what may reasonably be regarded as the value of the said benefit; and

- b. the Contractor shall not grant any licence for which there is no consideration, or only nominal consideration, without first agreeing with the Ministry what levy if any should reasonably be paid to the Ministry in respect of such licence; and
 - c. where the licensee pays for parts supplied in addition to paying its licence fee for manufacturing Contract Articles, levy on such parts shall be due in accordance with Clause 2 above in addition to the rate due under this clause. The receipts by the Contractor in respect of such parts shall not be regarded as receipts in respect of the licence on which the levy of **(Information Redacted)** per cent is charged.
4. Payment of levy is deemed to include payment for the use of any industrial property rights owned by the Ministry in connection with a sale or other transaction giving rise to levy under this Agreement.
5. No levy shall be payable in respect of:
- a. purchases by the Ministry;
 - b. sales to another UK Government Contractor or sub-contractor when the Contract Articles concerned can be clearly identified as being supplied to meet the requirements of the Ministry;
 - c. substantial individual equipment not developed at UK Government expense.
6. In the case of sales to the **(Information Redacted)**, whether directly or under a sub-contract, of Contract Articles which are **(Information Redacted)**, Woomera, and of spares for elements of such systems, the levy shall be restricted to a charge for the use of Government-funded tooling in accordance with Clause 2.b.

Sales of or Licensing of Spares or Parts

7. The sale of or licence to manufacture spares or parts of Contract Articles shall attract levy in accordance with this Agreement unless the Ministry agrees that an allowance may be made for any elements of the design of any such spare or part that were not developed at UK Government expense or a reduced rate of levy shall apply on all such spares and parts where there are practical difficulties in distinguishing between those which attract the full rate of levy, those which attract a reduced rate of levy and those on which no levy is due.

Derivatives

8. Should the Contractor sell, refurnish, recondition, maintain, lend, hire, or grant a licence to manufacture any articles in any further stage of development or articles based on the design of, or using design features of, or being a scaled version of, the Contract Article, levy calculated in accordance with this Agreement shall be due to the Ministry only to such extent as shall be reasonable in the circumstances. Subject to this the provisions of this Agreement shall apply.

Refurbishing or Reconditioning

9. Should the Contractor for resale or otherwise refurbish or recondition any Contract Articles (except at no charge to the customer under defects liability obligations) the Contractor shall pay to the Ministry a levy consisting of:

- a. a sum calculated in accordance with this Agreement on the selling price of any new sub-assemblies, components and spare parts embodied in the reconditioned or refurbished Contract Articles; and
- b. a sum for any use of Government-funded tooling (other than any used only in the manufacture of the said new sub-assemblies, components and spare parts) calculated as in Clause 2.b on the Contractor's selling price of the said reconditioned or refurbished Contract Articles after deduction of the selling price of any new sub-assemblies, components and spare parts embodied in the reconditioned or refurbished Contract Articles.

Maintenance Agreements

10. Where an agreement for the maintenance of Contract Articles between the Contractor and another party for a fee includes the provision of parts and spares of such Contract Articles not separately invoiced, a levy calculated in accordance with this Agreement will be due on that proportion of the maintenance fee which represents a reasonable estimate for the provision of such parts and spares.

Loan or Hire of Contract Articles

11. Should the Contractor enter into any Agreement for lending any Contract Articles or for otherwise making such Articles available to a third party except by way of sale, the Contractor shall pay to the Ministry a levy calculated as specified under Clause 2 hereof of the gross receipts of the Contractor.

Provided that:

- a. where the consideration consists wholly or in part of some benefit other than money the levy shall, in lieu of or in addition to such payment (as the case may be), consist of or include a sum calculated in accordance with Clause 2 hereof and based on what may be reasonably regarded as the value of the said benefit; and
 - b. the Contractor shall not enter into any Agreement (as set out in this clause) for which there is no consideration, or only nominal consideration, unless the Ministry has agreed what levy, if any, should reasonably be paid to the Ministry in respect of such Agreement.
12. Unless the Contract Article is subsequently sold, no levy shall be due where the Contractor makes a Contract Article solely for its own research or development purposes or for its own demonstration or sales promotion purposes, except in respect of use of Government-funded tooling. Contract Articles made and used by the Contractor for any other purpose shall attract levy at normal rates in accordance with Clause 2.

Abatement of Levy

13. Where, in the circumstances of an individual sale, the Contractor considers that the effect upon its selling price of inclusion of levy rates calculated in accordance with Clause 2 would be such as to prejudice its chances of completing the sale, or would result in an unreasonably low profit, it shall be open to the Contractor before the sale contract is entered into to seek the approval of the Ministry to an abatement scheme in accordance with the provisions of Clauses 14 and 15 herein. Provided that the Contractor's cost accounting system is adequate in the opinion of the Ministry to provide the statements of allowable costs

necessary to implement the scheme such approval will not be unreasonably withheld.

14. The abatement scheme shall generally determine levy on the basis of outturn profitability of the sale in question expressed as a percentage on the allowable costs as prescribed for this purpose by the Ministry and shall apply as follows:

- a. where Government-funded tooling is used, the first half percent of profit on cost shall be payable to the Ministry;
- b. the next **(Information Redacted)** of profit on cost (or the initial **(Information Redacted)** where sub-clause 14.a does not apply) shall be retained by the Contractor;
- c. the remaining profit, without upper limit, shall be shared between the Ministry and the Contractor in the ratio of 1:1 until a total profit of **(Information Redacted)** on cost has been reached, and thereafter in the ratio of X:1.

Note: X should be one-fifth of the total normal unabated levy rates, but never less than 1.

15. Once a request to apply the abatement scheme has been approved by the Ministry it shall not thereafter be revoked by either party for the sale in question. The Contractor shall provide on request and in a specified form a certified statement of costs and profitability and such facilities as may be necessary for the Ministry, if it so desires, to verify the statements. Where the value of the sale is less than **(Information Redacted)** any abatement of levy may at the discretion of the Ministry, be settled (before the sale contract entered into is concluded) on the basis of the expected outturn profitability provided the request for abatement is supported by adequate evidence and reasonable notice is given to the Ministry.

Notification of Leviable Transactions

16. The Contractor shall notify details including, where appropriate, the expected value of the sale, to the Ministry Delivery Team named in the Contract quoting the number of the Contract / CEL Agreement No.:

- a. in respect of a sale of any Contract Articles or of a development or derivation thereof:
 - (1) as soon as it becomes apparent that a sale (or contemporaneous sales of the same equipment to the same customer) above **(Information Redacted)** in value (or such higher value as may be notified by the Ministry from time to time) may arise;
 - (2) immediately a first sale of lesser value is entered into;
- b. immediately any negotiations for the grant of a licence for the manufacture of any Contract Articles, or of a development or derivation thereof, is entered into (the Ministry reserves the right in this connection to be supplied with a copy of the terms of the licence agreement); or
- c. in respect of any leviable transaction other than a sale or licence relating to any Contract Articles, or to a development or derivation thereof:

- (1) immediately the transaction is entered into where the rate of levy is laid down in this Agreement;
- (2) immediately negotiations are entered into where the appropriate rate of levy has not been agreed;
- d. when any proposed extension or alteration to the transactions set out in a.(1), b. or c.(2) is considered.

Cancelled Orders

17. Where a sale is cancelled after some work in aid of the sale involving the use of Government-funded tooling has been undertaken, a levy shall be due in respect of such use calculated on a fair and reasonable basis. Where the Contractor has received any payments, whether from its customer or otherwise which it is entitled to retain, in respect of work done or in hand, or in respect of any claim arising out of the cancellation, levy shall also be due on a fair and reasonable basis having regard to the reasonable costs and claims which the Contractor may have to meet therefrom. The Contractor shall notify any such cancellation to the Ministry Delivery Team named in the Contract and shall provide such information as may reasonably be required for the determination of the levies payable under this Clause. Should any Contract Article (or article falling under Clause 8) manufactured or in course of manufacture prior to cancellation subsequently be re-sold levy will again be due on the normal basis.

18. The liability of the Contractor to the Ministry for any sum due under this Agreement shall accrue:

- a. in respect of sales, on the date of delivery ex-Contractor's works or, where the sale contract so prescribes, upon shipment;
- b. in respect of cancelled sales, six months after the date of cancellation or such longer period as may be agreed;
- c. in the case of licences, and in any other case in which levy is based on gross receipts by the Contractor in respect of an agreement relating to Contract Articles, on the date of receipt by the Contractor of each payment;
- d. in respect of the use of Government-funded tooling where no other liability for levy arises, upon completion of the work in question, except that if the work takes longer than a year interim payments of levy will accrue as deliveries take place. In the event of cancellation of the sale liability will accrue six months thereafter;
- e. in respect of any Variation of Price settlements on receipt of payment by the Contractor.

Payment of levy shall be in accordance with the Accounting provisions at Clauses 21-24 below.

19. Where an abatement scheme has been approved in accordance with Clauses 13-15 the Contractor shall be liable for interim payment of levy in accordance with the provisions of Clause 18 at one half the appropriate unabated levy rate unless the Ministry agrees otherwise. A final adjustment to or from the Ministry shall be made as soon as it is practicable after completion of the sale. The Ministry reserves the right to review and alter interim rates of levy from time to time and agrees to carry out such a review upon request by the Contractor.

20. Should the Contractor fail to provide statements under Clause 22 within a reasonable time the Ministry reserves the right to assess the levy payable and to recover the same.

Accounting

21. The Contractor shall supply to Defence Business Services Finance-Commercial Exploitation Agreement Team, 1st Floor, Walker House, Exchange Flags, Liverpool L2 3YL, two copies of a statement (see Clause 22) at [.....] intervals commencing with first sale or licensing arrangements (see Clause 16).

22. The statement shall contain information concerning every sale, licence or other transaction in respect of which levy accruing during the period to which the statement relates is payable, and in particular shall specify:

- a. the nature of the transaction (making clear under which of the Clauses 2-12 hereof it falls) and the date thereof and the name and address of the other party or parties thereto;
- b. in the case of a sale, the quantity and type of equipment sold, the selling price, and in any other case, the gross receipts in money in respect thereof and the nature and value of any consideration other than money;
- c. any other matters relevant to determining the levy payable;
- d. the sum (to the nearest pound) computed to be payable by the Contractor to the Ministry in respect of each transactions (including a provisional sum in any case in which the sum depends upon a reasonable figure yet to be agreed with the Ministry).

23. The statement shall be provided not later than two months after the close of the period to which it relates once a first sale or licensing has been agreed and 'nil' statements shall thereafter be provided whenever appropriate. Where there are NIL returns over a number of years and no evident prospect of a future leviable activity or receipt the contractor should approach the Ministry Delivery Team commercial officer regarding future reporting and future CEL arrangements.

24. Each statement shall be accompanied by a payment covering the accrued levy calculated by the Contractor to be due and set out in the statement (plus VAT where applicable). Invoices in respect of any other accrued levy will be issued to the Contractor by Defence Business Services Finance-Commercial Exploitation Arrangement Team (DBSFin-CEA-Team@mod.uk). Payments (including VAT where applicable) shall be made to the Secretary of State for Defence at the address to which statements are to be supplied, or at the address stated on the invoice, as appropriate.

25. Two copies of an annual certificate that the sums reported on the statements are correct and complete and in accordance with the Contractor's books of account and records or that no sales have been made or licences granted or other leviable transactions entered into, shall be obtained by the Contractor from its Auditors and shall be forwarded to Defence Business Services Finance-Commercial Exploitation Arrangement Team (DBSFin-CEA-Team@mod.uk) not later than six months after the end of the Contractor's financial year.

26. For the purpose of verifying the statements the Contractor shall maintain proper books of account and records at its premises and shall make them available for inspection at all reasonable times by the representatives of the Ministry and of the National Audit Office.

Recovery of Sums Due

27. Whenever under this Agreement any sum of money shall be recoverable from or payable by the Contractor, the same may be deducted from any sum then due, or which at any time thereafter may become due, to the Contractor under any contract with the Ministry or with any Department or Office of Her Majesty's Government.

Arbitration etc

28. This Agreement shall be considered as an agreement made in England** and subject to English Law**.

29. All disputes, differences or questions between the parties to this Agreement with respect to any matter arising out of or relating to this Agreement shall be referred to the arbitration of two persons (one to be appointed by the Ministry and one by the Contractor) or their Umpire, in accordance with the provisions of the Arbitration Act 1996.**

(** Amend as necessary should Scots Law apply - the revision should be modelled on DEFCONs 529A and 530A, omitting from the latter references to other conditions and matters on which the MOD's decision is final.)

30. Nothing in this Agreement shall be construed as relieving the Contractor from responsibility for:

- a. obtaining the necessary export licence as applicable to any overseas sale;
- b. obtaining any necessary release from security restrictions in force for the Contract Articles.

31. Contractors are advised to consult the Exports Team, Security Policy and Operations, MOD, 4.C, Whitehall, London SW1A 2HB, on a case by case basis before making offers to sell Contract Articles overseas.

Signed:
(MOD Commercial)

Signed:
(Contractor)

Date:

* Delete words in parentheses as appropriate