

## Problem for the Fifth Annual Intercollegiate Negotiation Competition

1. Negoland is a republic with a population of approximately 7 million people and a GDP of approximately 200 billion US dollars. The country has a land area of approximately 300,000 km<sup>2</sup> (square kilometers), and has abundant forest and coal resources. In the past, the country had the three traditional major industries of coal, paper and pulp making, and metal, as its core, but after the 1980's it transformed into an industrially-advanced nation centering on the high-tech industry. The real GDP growth rate has been steadily advancing at a 3 - 6% level for the past five years. The currency is the Nego-Dollar (one Nego-Dollar is deemed to be equivalent to one yen). Negoland is internationally famous for its superior education system and solid welfare system. With respect to education, mandatory education for children from 6 to 16 years of age is free: and Negoland also has been making efforts to strengthen advanced research institutions. The state sets goals within the overall framework of the curriculum, but leaves the greater part of the educational content, such as the method of coursework composition and the selection of textbooks, to the discretion of the field staff. It is the main assessment among scholars that, as a result, educational institutions are competing to be creative, thus leading to improvement in the quality of education, and consequently resulting in the situation where a highly capable workforce that supports the high-tech industry is secured in a stable fashion. In addition, traditions of long-term employment and a well-established seniority system are viewed as contributing to a stable employment structure. In terms of welfare, the state's income security and pension program are at the highest level even among advanced nations, and health care is also basically free. Moreover, as a countermeasure to the falling birthrate, the state bears a fixed rate of the cost of raising children, and the state also has established a daycare system for children who are seven years old or younger. A high-standard system of childcare leave is recognized by law and is also utilized widely in practice. For a period of time in the past the falling birthrate was a problem in Negoland, but the systems such as those mentioned above proved effective, and currently the falling birthrate issue has been solved. To support this generous system of social services, the consumption tax stands at the high level of 30%, but the citizens support the policy of high obligations and strong welfare. The concept of equality between the sexes is thoroughly enforced. That, coupled with the daycare system for small children, helps account for an employment rate for women between the ages of 25 and 54 of approximately 80%. The rate of female managers is approximately 30%, and the view exists that the performance by women in the workplace is another factor underlying the economic growth of Negoland.
2. Negoland's neighboring country, Arbitria, is a state under parliamentary democracy with a population of approximately 50 million people and a GDP of approximately 600 billion US dollars. The country's land area is approximately 150,000 km<sup>2</sup>, and it has much flat land. The main industries include automobiles, steel, chemicals, and machinery. The currency is the Arb (one Arb is deemed to

be equivalent to one yen). Arbitria has been flourishing, centering on its industries, since the latter half of the 19<sup>th</sup> century. Companies in Arbitria are generally known for their high technical capabilities, and, especially in fields such as automobiles, chemicals and electric machines, Arbitria has spawned some of the world's leading companies. The high technological capabilities of Arbitria's industries are said to be supported by the advanced mandatory education. Mandatory education in Arbitria is provided for children from 6 to 18 years of age, and the government has been determining the educational content by taking the initiative in an effort to provide education that is more advanced than that in any other advanced nation. Particularly with respect to math and science, by the time students in Arbitria reach the age of 18, they are expected to have mastered content equivalent to that which is taught in general education courses at universities in Japan. There is some criticism that this constitutes cram education, or that this has become standardized education with no flexibility at the school level, but many citizens believe that Arbitria is being sustained by the advanced education system, and therefore they are supportive of the current structure. However, Arbitria has experienced great hardship in recent years. As in Japan, a bubble economy with a background of abnormal increases in real property and stock prices had developed, and after building up for ten years this bubble burst in 1990. For ten years after that, Arbitria's economy suffered from a situation of non-performing loans of financial institutions, together with a rapid increase in bankruptcy and loss of employment. Throughout those ten years, the rate of economic growth also was negative; but recovery started in 2000, and a 1-3% level of economic growth has been secured for the past five years. Currently, the social security system has become a major social issue in Arbitria. In Arbitria, serious aging of society is progressing, and the proportion of people over 65 years of age in the population has been increasing by 0.5% each year for the last twenty years, reaching approximately 20% in 2006. On the grounds that under such a serious aging of society it has become difficult to maintain the existing pension program and healthcare insurance system, the Arbitrian government announced two years ago its plan to fix the current state of pensions by no longer providing any increase corresponding to rises in the cost of living, and also, in relation to the healthcare insurance system, to increase the rate of payment of out-of-pocket medical expenses for people over 65 years of age from 10% to 30%. Currently, countermeasures relating to the aging of society and reform of the social security system have been discussed by the government, etc., but no drastic solution has been put forward. The social advancement of women is progressing, but many companies in Arbitria remain centered on men. In Arbitria, the Law on Equal Employment Opportunities for Men and Women came into force five years ago (the gist of the Arbitrian Law on Equal Employment Opportunities for Men and Women is as provided in Attachment 1), but the average employment rate for women between the ages of 25 and 54 is at about the 40% level, and the rate of women managers is at about the 10% level. From an international perspective, these rates remain low.

3. The neighboring countries Negoland and Arbitria are currently in an extremely close economic relationship. Both countries have been the mutual top trade partner of the other in relation to both

exports and imports for the last five years. Two years ago, they entered into a new tax treaty in an effort to further energize the investment flow between the two countries (the tax treaty between Negoland and Arbitria is exactly the same as the current OECD model tax treaty, and consultations aimed at the for the execution of Free Trade Agreement (FTA) commenced last year. (The status of trade between Negoland and Arbitria is as set forth in Attachment 2.) Despite the current close economic ties, there was an unhappy period of time in the relationship between these two countries. From 1941 to 1942, there was a war between the two countries. During that period, both Negoland and Arbitria had fallen into serious depression in the midst of the global Great Depression. Under these circumstances, totalitarian and nationalist ideas gained power in Arbitria, and a fascist political party came into power. As a result, Arbitria was internationally isolated, and embargoes of resources such as oil and coal were imposed against Arbitria. Arbitria, which had no resources such as oil and coal, was cornered, and attacked the neighboring country of Negoland to obtain coal resources. Arbitria was on the offensive for the first year, but after that year passed, Negoland, which had gained support from many advanced nations (they were being called the Allies), went on the counterattack, and finally, two years after the start of the war, Arbitria surrendered unconditionally. For five years thereafter, Arbitria was under occupation by the Allies, but it entered into a peace treaty with each of the Allied nations, including Negoland, in 1948. Subsequently, Arbitria achieved development as a democratic nation, and the relationship with Negoland also improved, leading to the present situation of good relations between the two countries.

4. Red Industries, Co. (hereinafter Red Co.) is an electronic components manufacturer in Negoland. Red Co. was established in 1950 by Mitsuru Red, who is the parent of Fan Red, the current chair of the board of directors. Mitsuru secured employment with a Japanese company after studying at a Japanese university as a foreign student, and gained knowledge and technical skills with respect to electronic components. Afterward, he returned to Negoland and started the business of Red Co. Initially, Red Co. began as a small electronic components business, and later it started handling transistors, diodes, etc. from the latter half of the 1960s. From the 1970s Red Co. expanded operations and began handling semiconductor elements, such as integrated circuits. Since then, Red Co. has grown steadily, moving in step with the flow of the development of Negoland since the 1980s. With the progress in science and technology, Red Co. promoted the development of integrated circuits since the 1990s, and has expanded its business performance. Now, since the start of the new millennium, Red Co. is advancing into the display field, aiming for further expansion. Currently, Red Co. consists of three departments: the Integrated Circuit Department, with representative products being the system LSI (large-scaled integrated circuit) used for mobile phones and audio-related equipment; the Semiconductor Element Department, responsible for products such as transistors and light-emitting diodes (LED); and the Display Department, responsible for products such as liquid crystal (LC) and LED displays. In all of these departments the products of Red Co. are highly evaluated internationally and are performing steadily. The current chair of the board of directors, Fan,

assumed the position upon Mitsuru's retirement in 1990. The motto of Red Co. is "Quality First", and this company motto is displayed, in the handwriting of the founder, in all offices and factories of Red Co.. Red Co. is also actively dealing with environmental issues by in accordance with ISO14001. The outline of Red Co. is provided in Attachment 3.

5. Blue Electronics, Inc. (hereinafter Blue Inc.) is an electric equipment manufacturer in Arbitria. Blue Inc. was established in 1935. When it was first established, the company had audio equipment such as radios and, later, televisions as its core, but it subsequently also advanced into home electric appliances such as refrigerators, microwaves, and air conditioners. Blue Inc. has gained a strong reputation both nationally and internationally as a general home electric appliance manufacturer, and its business performance is also steady. From about twenty years ago, Blue Inc. has been making inroads into the manufacturing of information and communication equipment such as personal computers. In addition, Blue Inc. is working on manufacturing electronic components such as image sensors used for CCD cameras and LSIs for liquid crystals. Moreover, recently, with the increasing popularity of mobile phones in Arbitria, Blue Inc. has been placing emphasis on mobile phones, and it has achieved a position as the unchallenged leader in this field. It stands at the top in market share in Arbitria by, for example, presenting mobile phones with unique functions not found in the mobile phones produced by any of its competitors. The management principle of Blue Inc. is "Good Faith and Trust". In recent years, it has been dealing actively with environmental issues, and it is also making efforts in developing technologies that will contribute to the environment. Lately, it developed an environmentally friendly air conditioner, which reduces consumption of electricity to one third of that used by existing air conditioners and is made mostly of parts that are recyclable. This product won the home electric appliance Grand Prize in the 2005 Arbitria Eco Goods Contest. The outline of Blue Inc. is provided in Attachment 4.

6. Blue Inc. undertook the manufacture of mobile phones in earnest fifteen years ago. There are two mobile phone companies in Arbitria, Yellow Phone Ltd. and Purple Mobile Co. The outlines of Yellow Phone Ltd. and Purple Mobile Co., as well as trends in the number of mobile phone subscribers in Arbitria, are provided in Attachment 5. Three manufacturers supply mobile phones to Yellow Phone Ltd. and Purple Mobile Co. Blue Inc. is one of them, and it supplies to both Yellow Phone Ltd. and Purple Mobile Co. The other two companies that supply mobile phones are Black Electronics and White Technologies, Inc. Black Electronics supplies only to Yellow Phone Ltd., and White Technologies, Inc. supplies only to Purple Mobile Co. The volume of shipments for Blue Inc., Black Electronics, and White Technologies, Inc., respectively, is provided in Attachment 5. None of Blue Inc., Black Electronics nor White Technologies, Inc. is currently shipping mobile phones to places outside Arbitria. Moreover, due to peculiarities of the Arbitrian market, it is difficult for foreign mobile phone companies or foreign mobile phone manufacturers to newly enter into the market.

7. Blue Inc. obtains LSIs, which it uses for its mobile phones, from Red Co. Although Blue Inc. also manufactures electronic components such as LSIs for liquid crystals, it does not manufacture LSIs for mobile phones. Since Blue Inc.'s mobile phones are more multifunctional but consume less power than those of other companies, they have a special feature that offers 1.2 times longer talk-time compared to other companies. This special feature of Blue Inc.'s mobile phones is largely due to Red Co.'s LSIs, and having this special feature as an advantage, it has become possible for Blue Inc.'s mobile phones to proudly capture 50% of the market share in Arbitria. Red Co. has the capability to produce superior circuit designs, and at least at present, there is no other manufacturer anywhere in the world who can produce LSIs that are suitable for the needs of Blue Inc. Blue Inc. has been receiving LSI supplies from Red Co. ever since Blue Inc. first embarked on manufacturing mobile phones. In commencing the manufacture of mobile phones, Blue Inc. first approached the LSI manufacturers in Arbitria about LSI supply, and then extended its search to some of the leading foreign LSI manufacturers. However, the LSI which Blue Inc. had considered necessary for manufacturing the mobile phones that it thought ideal was considerably different from what each manufacturer had developed up to then. At that time, each manufacturer was emphasizing the development of LSI specifications that each company thought best, and was not very enthusiastic about custom-made LSIs corresponding to individual orders from individual customers. Thus, many manufacturers were reluctant to supply LSIs to Blue Inc. Red Co. alone responded to Blue Inc.'s seemingly impossible request and engaged in the development and manufacturing of LSIs for Blue Inc.'s mobile phones. This was largely a result of the personal relationship between Fan Red, the president of Red Co., and Dale Blue, the president of Blue Inc. When Fan was working for a Japanese company, Dale was being trained at the same Japanese company, and they lived in the same dormitory for two years. Fan appointed Red Co.'s best engineer for LSI circuit design to work on the project for Blue Inc., saying, "I will cooperate as much as I can if it is a request from Dale." In the end, Red Co. was successful in developing the LSI that Blue Inc. had requested. As a result, Blue Inc. has been purchasing from Red Co. all the LSIs that it incorporates into the mobile phones that it manufactures. Red Co. supplies LSIs for mobile phones to companies in Negoland and other countries, but does not supply LSIs for mobile phones to any mobile phone manufacturers in Arbitria other than Blue Inc.
8. With respect to the supply of LSIs, Red Co. and Blue Inc. executed an agreement five years ago, as set forth in Attachment 6, and subsequent to the execution of this agreement, the supply of LSIs between Red Co. and Blue Inc. has been conducted in accordance with this agreement. (Previously, a simple contract was created for each individual transaction, but a master agreement was entered because the volume of transactions had increased.)
9. Blue Inc. supplies mobile phones to Yellow Phone Ltd. and Purple Mobile Co., and currently it supplies MODEL YB-5 mobile phones to Yellow Phone Ltd. and MODEL PB-3 mobile phones to

Purple Mobile Co. The LSIs used for each model are different. MODEL YR-5 LSI is used for the MODEL YB-5 mobile phone, and MODEL PR-3 LSI is used for the MODEL PB-3 mobile phone. It is not possible to use YR model LSIs in PB model mobile phones, or PR model LSIs in YB model mobile phones. Both MODEL YR-5 and MODEL PR-3 cost 10,000 Arb each. It takes two weeks for Red Co. to manufacture LSIs after receiving an order, and this period cannot be shortened.

1 0. The development of technology in the mobile phone world is rapid. Companies in Arbitria are releasing new models with new functions one after the other. Blue Inc. has worked on the development of a new style mobile phone for Yellow Phone Ltd. since one year ago, in the fall of 2005. It is a mobile phone equipped with the function of simultaneous interpretation, which enables simultaneous interpretation from the Arbitrian official language, Arb, to six other languages, and from six different languages to the Arb language. For instance, if the user sets the mobile phone to the simultaneous interpretation mode for English and speaks in the Arb language, simultaneous interpretation is done inside the mobile phone and the speech is communicated to the other party as an English audio signal. Inversely, the English audio signal received from the other party is simultaneously interpreted inside the mobile phone, and is heard in the Arb language, audio-synthesized by a computer. Yellow Phone Ltd. had high hopes for this new model, viewing it as a product that would enable it to regain the market share that had been taken away by Purple Mobile Co. After commissioning a number of trusted research firms, Yellow Phone Ltd. found that, if it launches this new model, approximately 3 million people, out of those who were originally going to buy Purple Mobile Co.'s mobile phones, would purchase this new model. In that case Yellow Phone Ltd. would be able to gain 5 billion Arbs in profit. This projection, however, is based on the premise that Purple Mobile Co. will not launch mobile phones with a similar function for half a year. Furthermore, in the event the above projection is realized, the company that manufactures the mobile phone units would be able to gain 2.5 billion Arbs in profit. According to information from a reliable source, Purple Mobile Co. had once attempted to develop a new model with a similar function jointly with White Technologies, Inc., but was unable to overcome a technical problem and gave up.

1 1. Yellow Phone Ltd. named this new model Model X, and decided to move forward with the development of Model X under conditions of strict confidentiality. After examining such matters as technical expertise, Yellow Phone Ltd. decided to request Blue Inc. to handle the development of the mobile phone unit. Accordingly, on September 1, 2005, Blue Inc. and Yellow Phone Ltd. executed a development agreement, as set forth in Attachment 7, and have pushed the development of Model X. Even for Blue Inc., this constituted a large-scale project that, if successful, would bring a profit of 2.5 billion Arbs, but in developing this Model X it was necessary to develop a new LSI. Blue Inc. decided to ask Red Co. to develop the LSI for this project to Red Co. For this purpose, on November 1, 2005, Blue Inc. separately executed an agreement with Red Co., as set forth in Attachment 8. For this project, Blue Inc. seconded a specialized engineer to Red Co., and made the engineer the assistant

leader of the new LSI development team in Red Co. The leader of that team, an engineer of Red Co., was expected to direct the team with the cooperation from the assistant leader. Upon the secondment of this engineer from Blue Inc., the Employee Secondment Agreement set forth in Attachment 9 was executed between Red Co. and Blue Inc., separately from the agreement in Attachment 8.

1 2. Although the business between Red Co. and Blue Inc. had been progressing smoothly, two serious problems arose in the fall of 2006. The first was a problem concerning the MODEL PB-3 mobile phone of Purple Mobile Co. Purple Mobile Co.'s MODEL PB-3 was popular, and there were people who had been using Yellow Phone Ltd.'s mobile phones but switched because of their desire to use MODEL PB-3. These phones were therefore on back order even at the stores of Purple Mobile Co. Under these circumstances, Purple Mobile Co. decided to host mobile phone fair in various locations in the capital city, Arb, for three days from October 1, 2006, in an effort to take the offensive in one go. One purpose of this fair was to make the mobile phones of Purple Mobile Co. known more widely by using celebrities, etc. At the same time, another purpose was to secure the purchase of Purple Mobile Co.'s mobile phones by the base of customers who were thinking about upgrading their mobile phones and would purchase phones from Purple Mobile Co. if those phones were readily available, but otherwise would purchase mobile phones from Yellow Phone Ltd., by greatly increasing the production of the new model then on back order so that ample supplies would be ready for the fair.,. In June, Blue Inc. received from Purple Mobile Co. a large-volume order for 60,000 units of the MODEL PB-3, to be delivered in time for the fair. Blue Inc. ordered 60,000 units of MODEL PR-3 LSI from Red Co., and these LSIs were delivered in July as scheduled. Blue Inc. started the increased production of MODEL PB-3, and on August 20<sup>th</sup> production of half the order, 30,000 units, was completed. In order to meet the date for the fair, the delivery had to be made by September 20<sup>th</sup>. At the regular production pace, 1,000 units could be produced in one day, but since 1,200 units could be produced per day by increasing the speed of the machines by 20% from the regular pace, the pace was adequate to complete production in time. In fact, Blue Inc.'s machines can be operated up to a maximum pace of 50% over the normal pace.

1 3. Suddenly, however, during the night of August 20<sup>th</sup>, lightning hit the warehouse of Blue Inc., and the 30,000 units of the MODEL PR-3 LSI that had been stored in the warehouse were destroyed by fire. Blue Inc. immediately placed an order with Red Co. to purchase replacements. Red Co. should normally be able to deliver goods in two weeks after receiving the order if it responds with great urgency. According to Purple Mobile Co., it could manage to accommodate the delay up to September 25<sup>th</sup>, and thus 30,000 units would somehow manage to arrive in time for the fair if 30,000 units of the LSI were delivered on September 5<sup>th</sup>. The person who would be responsible for this matter in Blue Inc. was the GM (General Manager) of the Mobile Phone Business Department. On the other hand, the person who would be responsible for dealing with Blue Inc. on the Red Co. side was the GM of the Sales Department. Any important correspondence associated with mobile phones was

always carried out between these two people, and the authority to sign order forms and contractual documents also had been granted to them (in addition, the signing authority for order forms had been granted to the Deputy General Manager). The GM of the Mobile Phone Business Department of Blue Inc. phoned the GM of the Sales Department of Red Co. on August 21<sup>st</sup>, and explained the situation as follows: “As you may be aware, Purple Mobile Co. is planning to host mobile phone fair from October 1<sup>st</sup> to 3<sup>rd</sup>, and we must deliver 60,000 units of MODEL PB-3 in time for the fair. Last month we had 60,000 units of MODEL PR-3 LSI delivered from your company and had already completed the production of 30,000 units, or half of the order, but last night lightning hit our company warehouse, and the remaining 30,000 units of MODEL PR-3 delivered by your company in July were all destroyed by fire. We would like you to send us the replacement of 30,000 units of MODEL PR-3 immediately.” In response, the GM of the Sales Department of Red Co. said, “I am very sorry to hear about the fire. I understand the situation and I will give instructions to the person in charge to carry out the production immediately. Delivery should be made on September 5<sup>th</sup>. I will have to go to Europe on a business trip for one month leaving this afternoon, but I will let the Deputy General Manager know. Just in case, I would like you to fax an order form to the Sales Department as usual.” The GM of the Mobile Phone Business Department of Blue Inc. thanked him, hung up the phone, and instructed the Deputy General Manager to immediately prepare an order form and fax it to Red Co. However, the order form that the Deputy General Manager signed and faxed to Red Co., wrongly stated 30,000 units of MODEL YR-5. On the receiving end, the GM of the Sales Department of Red Co. instructed the Deputy General Manager saying, “We will receive an urgent fax from Blue Inc., and I would like you to deal with it with great urgency. Confirm with the factory to deliver the order absolutely by September 5<sup>th</sup>.” The GM of the Sales Department of Red Co. then left for Europe for one month on the business trip as previously scheduled. When the Deputy General Manager of the Sales Department received the fax from Blue Inc., the Deputy General Manager phoned the Deputy General Manager of the Mobile Phone Business Department at Blue Inc. and reported, “We confirm receipt of the urgent order form. It is for 30,000 units to be delivered by September 5<sup>th</sup>, is it not?” Later, when asked for testimony, the Deputy General Manager of Red Co. said that he stated at the time of this phone call, “It is for 30,000 units of MODEL YR-5 to be delivered by September 5<sup>th</sup>, is it not?” Conversely, the Deputy General Manager of Blue Inc. testified to having been told, “It is for 30,000 units of MODEL PR-3 to be delivered by September 5<sup>th</sup>, is it not?” Immediately after this phone call, the Deputy General Manager of the Sales Department at Red Co. made arrangements with the factory to commence the production of 30,000 units of MODEL YR-5 with great urgency, and the factory started the production of 30,000 units of MODEL YR-5 on that day. The Deputy General Manager reported to the GM of the Sales Department, then in Europe on his business trip, that, “We received an order form from Blue Inc., and I instructed the factory to commence production of 30,000 units immediately. I was told that we can make it on September 5<sup>th</sup>.” On the other hand, after faxing the order form to Red Co., the Deputy General Manager of Blue Inc. also filed the original order form in the order form binder and reported to the GM of the Mobile Phone Business Department that he had



confirmed the receipt with the Deputy General Manager of Red Co. by telephone. In past transactions, it was routine for Red Co. to return an order confirmation after receiving an order form from Blue Inc. This time, however, because things were chaotic given the urgent situation, and because the Deputy General Managers confirmed mutually on the phone immediately after placement of the order, the Deputy General Manager of Red Co. did not think of returning an order confirmation, and neither did Blue Inc. urge confirmation of the order.

1 4 . During the business trip in Europe, the GM of Red Co.'s Sales Department attended a tradeshow held in London at the end of August, and by chance met the GM of the Mobile Phone Business Department of Blue Inc., who was visiting the same tradeshow. There, the GM of Blue Inc.'s Mobile Phone Business Department said, "Thank you so much for the other day. There is no problem with the 30,000 units of MODEL PR-3, is there?", and the GM of the Sales Department of Red Co. said, "I was told by the Deputy General Manager that it has already been taken care of and also that we will make it in time for September 5<sup>th</sup>."

1 5 . On September 5<sup>th</sup>, 30,000 units of MODEL YR-5 were delivered to Blue Inc. Only then did Blue Inc. realize that the order form had wrongly stated 30,000 units of MODEL YR-5. The GM of Blue Inc.'s Mobile Phone Business Department hurriedly phoned the GM of the Red Co.'s Sales Department, but the GM was still away on the business trip in Europe. Instead, Blue Inc.'s GM talked to the Deputy General Manager, but was told, "Please check your order form. Our company sent the goods as requested on the order form, and we cannot do anything about it." This was not the first time an order had been placed with a mix-up between the items used by Yellow Phone Ltd. and the items for Purple Mobile Co. In 2004, there was an incident where, after a dialogue concerning an order for items to be used for Yellow Phone Ltd. was conducted orally between the GM of the Sales Department of Red Co. and the GM of the Mobile Phone Business Department of Blue Inc., just as this time, an order form for items to be used for Purple Mobile Co. was sent from Blue Inc. On that occasion, the GM of the Sales Department looked at this order form and noticed the difference from their previous conversation, and consequently had Blue Inc. resend a correct order form, thereby preventing any trouble from occurring. Moreover, it was not always the case that order forms were necessarily received for transactions in the past. There were other incidents with respect to transactions requiring urgency where an order was received over the telephone, to which Red Co. responded by immediately delivering the goods in stock, for which the order form was sent over after delivery. This occurred with orders for 5,000 units in 2003, 7,000 units in 2004, and 10,000 units in 2005.

1 6 . At the point in time when Blue Inc. realized a mistake had been made, it was clear that even if MODEL PR-3 LSIs were ordered, there would no longer be enough time to assemble MODEL PB-3 mobile phones in time for the fair, and the GM of the Mobile Phone Business Department of Blue Inc.

had no choice but to inform Purple Mobile Co. of the situation and explain that it could only deliver 30,000 units for the fair. The person in charge at Purple Mobile Co. was enraged, and demanded Blue Inc. to deliver the already completed 30,000 units, to have the remaining 30,000 units ready in stock so that orders from the customers at the fair would be filled promptly, and to compensate for all the losses that Purple Mobile Co. would suffer in relation to this incident.

1 7. In response to these exchanges with Purple Mobile Co., Blue Inc. sent an order form for 30,000 units of MODEL PR-3 to Red Co. with the letter in Attachment 10. To this letter, Red Co. responded by its letter in Attachment 11. Ultimately, on September 8, Red Co. and Blue Inc. agreed on the point that it was important to respond to the needs of Purple Mobile Co. at any rate for the present, and decided to ask for an opinion of a third party separately through arbitration with respect to the first 30,000 units; and, on September 30, Red Co. delivered the 30,000 additional units of MODEL PR-3. Moreover, with respect to the MODEL YR-5 units that had been delivered to Blue Inc., since Blue Inc., purely by good luck, received an order for MODEL YB-5 mobile phones from Yellow Phone Ltd., Blue Inc. decided to use the MODEL YR-5 units for producing the MODEL YB-5, and paid Red Co. 300 million Arbs for those units.

1 8. After the fair, Purple Mobile Co. demanded Blue Inc. to compensate for damages in the amount of 300 million Arbs. Purple Mobile Co. claimed that, because Blue Inc. did not deliver to Purple Mobile Co. the 30,000 units of Model PB-3 on the due date, Purple Mobile Co. suffered damages such as lost earnings in the amount of 300 million Arbs. This issue was referred to arbitration, with the place of arbitration in Arbitria, and an arbitral award allowing all the claims of Purple Mobile Co. was rendered.

1 9. Red Co. delivered 30,000 units of MODEL PR-3 in accordance with the order from Blue Inc., and requested payment. However, Blue Inc. asserted to Red Co. as follows: “Since Red Co. had been aware that what Blue Inc. was going to order was MODEL PR-3, based on the phone call between the GM of the Mobile Phone Business Department of Blue Inc. and the GM of the Sales Department of Red Co., Red Co. owed an obligation to Blue Inc. to deliver 30,000 units of MODEL PR-3 by September 5<sup>th</sup>, and delivering MODEL YR-5 despite this obligation amounted to default of its obligation. As a result of this, Blue Inc. was forced to pay 300 million Arbs to Purple Mobile Co., and suffered damages in the same amount. Therefore, we offset the 300 million Arbs for MODEL PR-3 with the current request for payment of 300 million Arbs.” In response, Red Co. denied the assertion of Blue Inc., stating, “*In* accordance with our agreement, our company delivered the goods that were ordered through the order form we received, and there no default of an obligation occurred.” (Hereinafter, this first issue is referred to as the “Purple Mobile Incident.”)

2 0. The second problem concerned the development of Model X by Yellow Phone Ltd. In relation

to the development of a new style LSI in the course of the development of Model X, one employee had been seconded from Blue Inc. to Red Co., and the development work had been carried out by forming a project team within Red Co. This seconded employee of Blue Inc. was conducting the development of the new style LSI central to the project by cooperating with the staff of Red Co. As may be expected from the fact that Purple Mobile Co. and White Technologies, Inc. had previously failed in their attempt to develop such a product, the work of development at Red Co. faced tough going. However, technical issues were finally overcome in early September 2006, and the completion of a trial product was reached. The employee on the project seconded from Blue Inc. prepared a report concerning the overcoming of problems and the completion of a trial product, and sent the report to Blue Inc. This was good news for the Mobile Phone Business Department of Blue Inc. which had been in a slightly depressed mood due to the incident with Purple Mobile Co. As of early September, the technology related to the new style LSI had reached the stage where it would have been possible to file patent applications; but, just to be certain, Red Co. and Blue Inc. agreed to file the patent application after conducting a few more tests. (This technology is that referred to as the “Joint Technology” in the agreement set forth in Attachment 8.) In addition, Yellow Phone Ltd. and Blue Inc. agreed to file patent applications related to the technology for producing the corresponding newly developed mobile phone units, based on the same timetable. (This technology is that referred to as the “Joint Technology” in the agreement set forth in Attachment 7.)

2 1 . In early October however, Yellow Phone Ltd. contacted Blue Inc. and demanded, “We would like you to explain why the information on Model X is being disclosed on the Internet.” When Blue Inc. immediately checked, it found that the report prepared for Blue Inc. by its seconded employee to Red Co. was being disclosed on a Website on the Internet. When Blue Inc. hastily contacted Red Co. to check on the situation, it received a reply from Red Co. stating that, “Your company’s seconded employee prepared a report on the progress of the project for Blue Inc. on his personal computer and stored the file on the same computer, but it seems that the file leaked out through file exchange software this employee had used. It appears that the information leak occurred sometime in mid-September.” From the perspective of information management, Red Co. has a regulation prohibiting the use of personal computers with respect to the preparation of documents, etc., containing confidential information. As a result of the investigation, it was learned that this seconded employee had purposely prepared a report on his personal computer, rather than a computer of Red Co., based on his desire to use the company letterhead of Blue Inc. with respect to reports for Blue Inc. Moreover, the date on which this report was prepared was a day when the offices of Red Co. could not be used due to repair work. There is a possibility that interested parties from both Purple Mobile Co. and White Technologies, Inc. have already downloaded this file. In the report leaked out on the Internet, there was a reference to the core part of the technology of Model X, and the content was such that both Purple Mobile Co. and White Technologies, Inc., who already have experience in working on a similar project in the past, would in no time understand what the problem was by looking at this

report, and would be able to prepare a trial product immediately. Yellow Phone Ltd. was furious, and demanded Blue Inc. to investigate the facts of the situation with utmost urgency.

2 2. In late October, Purple Mobile Co. announced that it was going to launch mobile phones with the function for simultaneous interpretation in January of the following year. It has been learned that, in mid-October, Purple Mobile Co. and White Technologies, Inc. jointly filed applications for several patents relating to the new style mobile phone units and the LSIs those mobile phones contain, in a number of nations, including Negoland and Arbitria. Those patent applications treat the information leaked over the Internet as public knowledge, and relate to the invention which improved that technology. Yellow Phone Ltd., Blue Inc. and Red Co. suspended the planned additional tests and filed applications for the technology developed for this project, but those applications were rejected as lacking novelty, based on the applications previously filed by Purple Mobile Co. and White Technologies, Inc. Yellow Phone Ltd., Blue Inc. and Red Co. challenged these determinations in the relevant courts, but they lost all of those cases. In addition, Yellow Phone Ltd., Blue Inc. and Red Co. filed civil lawsuits in Arbitria against Purple Mobile Co. and White Technologies, Inc., claiming that those companies unfairly used confidential information belonging to Yellow Phone Ltd. et al. However, in part because access to information possessed by other parties is limited under the Arbitria Civil Procedure Code, Yellow Phone Ltd., Blue Inc. and Red Co. were unable to obtain sufficient information to prove that Purple Mobile Co. and White Technologies, Inc. utilized the information leaked over the Internet in developing and manufacturing new style mobile phones, and lost that case.

2 3. There is a confidentiality provision in the agreement between Yellow Phone Ltd. and Blue Inc. concerning the development of Model X, and there is a provision concerning liquidated damages compensation under which Blue Inc. is to pay 500 million Arbs to Yellow Phone Ltd. in the event Blue Inc. breached its confidentiality obligation. This agreement concerning liquidated damages did not exist in the initial draft of the agreement, but was requested by Yellow Phone Ltd. in the final stage of negotiations. Initially, the sum suggested by Yellow Phone Ltd. was 2.5 billion Arbs, but Blue Inc. insisted that there was no way it could accept a clause for liquidated damages of such a large sum. Yellow Phone Ltd., on the other hand, insisted that a clause for liquidated damages was indispensable, and during their negotiations they came to an agreement on the sum of 500 million Arbs. After the defeat in the civil case against Purple Mobile Co. and White Technologies, Inc., mentioned above, Yellow Phone Ltd. demanded payment of 500 million Arbs from Blue Inc., based on this provision. and When Blue Inc. consulted with their regular attorney, the attorney said, “ It is a fact that the information leaked, and, regardless of the result in the lawsuit against Purple Mobile Co. and White Technologies, Inc., you can’t escape liability under this provision,” so Blue Inc. paid 500 million Arbs to Yellow Phone Ltd.

2 4. Blue Inc. next turned to Red Co. Blue Inc. claimed that, since the seconded employee was

stationed at Red Co., and the incident arose in the course of work being conducted by this employee under the management of Red Co., Red Co. breached its confidentiality obligation under the agreement between Red Co. and Blue Inc. Accordingly, Blue Inc. sought payment from Red Co. of the 500 million Arbs which Blue Inc. had already paid to Yellow Phone Ltd., as the loss suffered due to the above circumstances. Red Co. refused the demand from Blue Inc. on the grounds that this case arose from the negligence of the employee seconded from Blue Inc. and was not something for which Red Co. should assume liability, and further that there was no evidence that Purple Mobile Co. or White Technologies, Inc., saw the file, nor was there any cause and effect relationship between the leakage of the file and the loss suffered by Blue Inc. (Hereinafter, this second issue is referred to as the “Yellow Phone Incident.”)

< Round A >

Although Red Co. and Blue Inc. explored means of solving their issues through negotiation, they failed to reach an agreement, partly because of the large sums involved. Ultimately, they decided to seek settlement through arbitration with regard to both to Purple Mobile Incident. and the Yellow Phone Incident. According to the terms of reference submitted to the arbitral panel, the claims made by Red Co. in this arbitration are as follows.

- ① Blue Inc. shall pay to Red Co. 300 million Arbs for the additional MODEL PR-3 units delivered on September 30.
- ② Red Co. seeks confirmation that Red Co. does not have any liabilities to Blue Inc. with regard to the Purple Mobile Co. issue and the Yellow Phone Incident.

On the other hand, the claims made by Blue Inc. are as follows.

- ① Blue Inc. seeks confirmation that Red Co.'s right to demand payment against Blue Inc. for the additional 30,000 units of MODEL PR-3 delivered on September 30 ceased to exist as a result of the setoff of Blue Inc.'s right to claim compensation for damages against Red Co., and that Blue Inc. does not have any liabilities to Red Co.
- ② Red Co. shall pay to Blue Inc. 500 million Arbs as the damages suffered by Blue Inc. as a result of the breach of the confidentiality obligation owed to Blue Inc. under the agreement dated November 1, 2005 (Attachment 7).

Since the following three disputed issues will be examined at the hearing on December 2<sup>nd</sup>, the arbitrators have directed each party to submit statements, on or before a date to be designated separately, setting forth that party's assertions. .

- ① What liability does Red Co. have to Blue Inc. as a result of the exchanges between Red Co. and Blue Inc. on August 21<sup>st</sup>? Does Red Co. have the obligation to pay Blue Inc. 300 million Arbs in compensation as damages based on the default of such liabilities?
- ② Does Red Co. have any legal liability to Blue Inc. based on the fact that information concerning Model X leaked out on the Internet?
- ③ Assuming that some legal liability is owed by Red Co. with respect to the leak of information, how much compensation as damages should be paid by Red Co. to Blue Inc. based on the breach of such liability?

< Round B >

The troubles surrounding Yellow Phone Ltd. and Purple Mobile Co. have settled, and the relationship between Red Co. and Blue Inc. has returned to its original closeness. Under these circumstances, there was an opportunity for both representatives to meet and talk leisurely for the first time in a long while. In that meeting, opinions were exchanged as to what kind of relationship between the two companies would be desirable. During these exchanges, Fan of Red Co. told Dale of Blue Inc. that, "I am thinking of retiring soon, leaving the management with my eldest son, Alex. However, he is still not dependable, and does not seem interested in managing that much. Although I have heard this before, it is difficult to know when to retire." In response, Dale proposed to Fan one idea that he has had in mind for a while. That idea is the following. "Blue Inc. considers that it wants to make the mobile phone business grow. For that purpose, superior LSIs are absolutely essential. Thinking this way, it is desirable to have an environment in which the Integrated Circuit Department of Red Co. and the Mobile Phone Department of Blue Inc. can engage in business in better collaboration with each other. I am wondering if you would consider selling the Integrated Circuit Department of Red Co. to Blue Inc. In addition, our Electronic Components Department is a little weak, and I would like to make that Department grow as one of our pillars by uniting it with your company's Integrated Circuit Department." To this, Fan responded, "I understand that we may not be able to survive unless our two companies cooperate with each other closely. However, this is such a sudden idea, which I had never thought of, and I cannot say anything now. Also, the Integrated Circuit Department is indeed the smallest department in our company, but it is doubtful that selling off only one department is realistic. In terms of combining the know-how of our two companies concerning the mobile phone business, there are ways to create a joint venture company, or to execute a long-term joint business agreement." Dale said, "You are right. However, if you are also thinking about retirement, let us create an opportunity to think diversely about the relationship between the two companies prior to your retirement, and think of what the best choice is for both companies." Fan nodded.

After these exchanges between the heads of the two companies, a committee was established within each of Red Co. and Blue Inc. for examining and discussing the relationship between the two companies. The purpose of the committees is to discuss the basic framework for that relationship. If the committees can agree on some kind of basic framework, then such a framework can be designed to move forward to processes such as the preparation of a letter of intent, due diligence, and the preparation of a contract in accordance with their agreement. So as to enable the exchange of information needed for discussions regarding the basic framework, a confidentiality agreement has been entered into between the two companies covering the information exchanged and the deliberations themselves. Since the committees were established to consider issues such as transfer of business divisions, etc., the existence of these committees is confidential in each company. Only a handful of members selected by both presidents participate in the deliberations. In the case of both Red Co. and Blue Inc., the top member of the committee is Vice President (in charge of corporate planning and human resources) and the other members are the Senior Managing Director (in charge of Sales Department), the General Manager of Finance and

Accounting Department, the General Manager of Legal Department and the General Manager of Research and Development Department. . There have already been two meetings bringing together the committees of Red Co. and Blue Inc. The meetings so far have been viewed as brainstorming sessions, and work has been conducted first to try and list widely what options would be available, leaving for later any detailed examination of the advantages and disadvantages for both companies. As a result of this, the following four items have been raised as options.

- ① Red Co. transfers its Integrated Circuit Department to Blue Inc.
- ② Red Co. and Blue Inc. establish a joint venture company with respect to the mobile phone business.
- ③ Red Co. and Blue Inc. enter into an agreement for a long-term cooperative relationship.
- ④ No action is taken.

Already several meetings have been held for discussions concerning the specific contents of these proposals, and for exchanging information considered necessary for examining each proposal. The memorandum in Attachment 12 has been prepared jointly by Red Co and Blue Inc. as a document outlining these discussions up to this time.

At the meeting on December 3<sup>rd</sup>, it is expected that a final discussion at the committee level will be held with regard to which proposal is to be selected out of these four options, and if both committees reach an agreement on any of the proposals, then the proposal selected is to be presented to both presidents. Both presidents would be reluctant about selecting any option as to which the committee members at the center of the business are unable to agree, and thus, if no agreement is reached at the meeting on December 3<sup>rd</sup>, option ④ will be selected automatically. If both presidents agree on any of the proposals from ① through ③ above, the parties will prepare a letter of intent with the content of such proposal, and if necessary, will move on to matters such as due diligence. The deliberations this time concern the basic framework, before entering into more detailed matters.

The company law in both Negoland and Arbitria is exactly the same as the company law that came into force recently in Japan. Furthermore, neither country has any regulations which would prevent the effectuation of any of the proposals from ① through ③ above.

The anticipated agenda for December 3 is as follows:

- (1) The members of the respective committees for each of the companies will consult with the president of that company for about ten minutes. For about the first five minutes of this meeting, the members of the committee will report to the president regarding their plans for the negotiations. The president has instructed the members of the committee to prepare a preliminary memo, setting forth concretely the items on which agreement is to be sought in the negotiations (the objectives of the negotiations), to be submitted on or before a time to be designated in advance. The president has entrusted the committee members with responsibility for deciding on the plans for the negotiations and will not override the views of the committee at this meeting.
- (2) Thereafter, negotiations will be conducted.



(3) After the conclusion of the negotiations, members of the respective committees for each of the companies will provide a report of no more than five minutes to the president of that company. For a period of about ten minutes thereafter, the president will hold a consultation session with the committee members.

Main Content of the Law on Equal Employment Opportunities for Men and Women in Arbitria

- Prohibition of discrimination against women at each stage of employment management
  - Discrimination against women is prohibited with respect to recruitment and hiring, assignments, promotion, educational training, certain benefit packages, retirement, resignation and layoffs.
  
- Prohibition of layoff, etc., on the basis of pregnancy or childbirth
  - Rules providing marriage, pregnancy or childbirth as a reason for resignation are prohibited.
  - Discharge on the basis of marriage, pregnancy, childbirth or obtainment of leave for childbirth is prohibited.
  
- Exceptions concerning conditions applicable to women only and preferential treatment for women
  - While generally any treatment applicable to women only or treatment preferential to women is prohibited, a measure conducted with the specific purpose of eliminating the gap between men and women workers at the workplace is not illegal.
  
- State's support for positive actions
  - The state enforces consultation and other support for employers who take a positive corporate approach (positive actions) to eliminate the gap actually existing between men and women workers.
  
- Measures to be considered in relation to the undertaking of work by women workers
  - Employers have an obligation to manage their employees to prevent sexual harassment in the workplace
  
- Measures in relation to the maternal health management of women workers
  - Employers are obligated to secure time for pregnant or postpartum women workers to receive health guidance and health examinations, and to implement necessary measures so that such women workers may follow the instructions based on such guidance or examination.

• Trade volumes of Negoland and Arbitria

Unit of

Year	Arbitria → Negoland	Negoland → Arbitria
Year 2000	74.8	64.3
Year 2001	62.8	62.2
Year 2002	61.2	65.2
Year 2003	70.5	72.1
Year 2004	83.5	83.4
Year 2005	90.5	85.3

measurement: One hundred million US dollars.

• Major trade areas (2005)

(the rate (%) of imports and exports between two countries is indicated in parenthesis)

• Arbitria → Negoland:

Automobiles (48.5%), video equipment (TVs, videos, etc.) (27.6%), electric appliances (14.7%)

• Negoland → Arbitria:

Lumber (16.6%), paper and cardboard (9.5%), electronic components (8.4%)

Trade Name	Red Industries, Co.	
Main Branch	Negoland, Negonego	
Date of Establishment	March 15, 1950	
Capital	5 billion Nego (as of March 31, 2006)	
Representative	Board Chair and President	Fan Red
Shares	Unlisted	
Major Shareholders:	Fan Red	30%
	Other Red family members	50%
	Nego Bank, etc.	20%
Number of Employees	4,000	

Trends in business performance

	Year 2002	Year 2003	Year 2004	Year 2005	Year 2006
Integrated circuits	5,000	5,000	6,000	7,000	7,000
Semiconductor elements	12,000	13,000	14,000	14,000	15,000
Displays	14,000	15,000	15,000	15,000	16,000
Volume of sales	31,000	33,000	35,000	36,000	38,000
Cost of sales	19,000	18,000	19,000	20,000	24,000
Service and general administrative expenses	6,000	6,000	7,000	7,000	8,000
Business profit	6,000	9,000	9,000	9,000	6,000
Corporate taxes, etc.	2,000	3,000	3,000	3,000	2,000
Current net profit	4,000	6,000	6,000	6,000	4,000
Research and development investment	4,000	4,000	5,000	8,000	8,000
Depreciation allowance	5,000	5,000	5,000	5,000	5,000

Unit of measurement: ,million Negos.

Balance Sheet (as of March 31, 2006; unit of measurement: million Negos)

Liquid assets	Cash	28,000	Liquid liabilities	Bills payable, book debts	3,000
	Receivables	10,200		Unpaid corporate taxes	1,500
	Inventory assets	8,500		Unpaid expenses	1,200
	Prepaid expenses	600		Loans payable	6,000
	Total liquid assets	47,300		Total liquid liabilities	11,700
Fixed assets	Land	6,700	Fixed liabilities	Severance pay reserve	300
	Building	17,000		Total fixed liabilities	300
	Machines, fixtures	46,000	Capital	Capital	5,000
	Accumulated depreciation	-45,000		Capital surplus reserve	10,000
	Total fixed assets	24,700		Retained earnings	45,000
	Total assets	72,000		Total capital	60,000

Trade Name	Blue Electronics, Inc.
Headquarters	Arbitria, Ab-ab
Date of Establishment	May 23, 1935
Capital	15,000 million Arbs (as of March 31, 2006)
Representative	Director and President Dale Blue
Shares	Listed on the Arbitria Stock Exchange
Number of Employees	8,000

Trends in business performance

	Year 2002	Year 2003	Year 2004	Year 2005	Year 2006
AV equipment	40,000	44,000	44,000	42,000	52,000
Home electric appliances	28,000	32,000	36,000	34,000	38,000
Information and communication	41,000	38,000	47,000	50,000	60,000
Electronic components	35,000	34,000	33,000	32,000	30,000
Volume of sales	144,000	148,000	160,000	168,000	180,000
Cost of sales	108,000	110,000	120,000	125,000	135,000
Service and general administrative expenses	28,800	29,000	31,000	33,000	37,000
Business profit	7,200	9,000	9,000	10,000	8,000
Corporate taxes, etc.	4,800	3,500	4,000	4,000	2,500
Current net profit	3,000	5,500	5,000	6,000	5,500
Research and development expenses	11,000	12,000	12,000	13,000	13,000
Depreciation allowance	12,000	11,000	13,000	12,000	12,000

Unit of measurement: million Arbs

Balance Sheet (as of March 31, 2006; unit of measurement: millionArbs)

Liquid assets	Cash	30,000	Liquid liabilities	Bills payable, book debts	59,000
	Receivables	40,000		Unpaid corporate taxes	3,000
	Inventory assets	30,000		Unpaid expenses	5,000
	Prepaid expenses	10,000		Loans payable	12,000
	Total liquid assets	110,000		Total liquid liabilities	79,000
Fixed assets	Land	20,000	Fixed liabilities	Severance pay reserve	1,000
	Building	20,000		Total fixed liabilities	1,000
	Machines, fixtures	70,000	Capital	Capital	15,000
	Accumulated depreciation	-60,000		Capital surplus reserve	20,000
	Total fixed assets	50,000		Retained earnings	45,000
	Total assets	160,000		Total capital	80,000

Subscribers of mobile phones, by year.

Unit	of	Year 2001	Year 2002	Year 2003	Year 2004	Year 2005
	Yellow	1,000	1,200	1,400	1,600	1,700
	Purple	500	700	900	1,000	1,300
	Total	1,500	1,900	2,300	2,600	3,000

measurement: ten thousand cases.

Outline of major mobile phone companies

- Yellow Phone Ltd. is a large telecommunications carrier holding 80% of the market share in Arbitria with regard to fixed telephones.
- Purple Mobile Co. is a mobile phone specialized company belonging to a large-scale corporations group in Arbitria. Its biometric service introduced in 2005 is booming and the company is expanding its market share.
- Up to the present, customers have had to change their phone numbers when they transfer a contract from Yellow Phone Ltd. to Purple Mobile Co., but, starting in 2007, contract transfer will become possible without phone number change, and thus the competition for customers between Yellow

	Year 2001	Year 2002	Year 2003	Year 2004	Year 2005
Blue	400	500	600	700	1000
(portion for Yellow)	250	300	350	500	400
(portion for Purple)	150	200	250	200	600
Black	200	250	300	400	500
White	200	250	300	400	500
Total	800	1000	1200	1500	2000

Phone Ltd. and Purple Mobile Co. is anticipated to escalate further.

Volume of new sales by mobile phone manufacturers

Unit of measurement: ten thousand units





SUPPLY AGREEMENT

THIS AGREEMENT, made and entered into as of this 1st day of April, 2001, by and between Red Industries, Co. ("Seller"), a Negoland corporation, and Blue Electronics, Inc. ("Buyer"), an Arbitria corporation.

WITNESSETH:

WHEREAS, Buyer is desirous of purchasing from Seller certain LSIs and of assembling those LSIs into mobile phones to be produced and sold in the name of the Buyer in Arbitria, and

WHEREAS, Seller is willing to supply such components to Buyer under the terms and conditions herein contained,

NOW, THEREFORE, in consideration of the mutual promises set forth herein and the mutual covenants herein contained, both parties hereto agree as follows:

1. ORDERS

- (1) During the term of this Agreement, Buyer shall from time to time will place orders for Products with Seller (each an "Order") in the form attached as Exhibit 1. The word "Products" in this Agreement shall mean LSIs produced by Seller, as specified in Exhibit 2 in more detail.
- (2) Once an Order is placed by Buyer, Seller shall use its commercially reasonable efforts to fill such Order as promptly as practical in accordance with the terms of such Order.
- (3) Price of the Products shall be as specified in Exhibit 2.

2. DELIVERY

- (1) Seller shall deliver the Products ordered by Buyer on the basis of CIF, such port in Arbitria as designated by Buyer at least three weeks before the commencement of time for shipment. The trade term CIF, as used herein, shall be interpreted in accordance with INCOTERMS 2000.
- (2) As a condition precedent to recovery for any claim for shortages, defects or other non-conformity in filling an order, Buyer must inspect the Products and make claim in writing, specifying any non-conformity, within fifteen (15) days after receipt of such Products at the

port of destination designated in accordance with the preceding paragraph (1).

(3) In the event Buyer defaults in any payment to Seller or otherwise defaults in the performance of this Agreement, Seller shall have the right, in addition to any other right or remedy, to suspend delivery of the Products ordered by Buyer but not yet shipped or to freely dispose of the same at Seller's discretion.

### 3. REPRESENTATIONS

Each of the parties represents and warrants to each other that:

- (1) it has a power to enter into this Agreement and to exercise its right and perform its obligations hereunder;
- (2) the obligations expressed to be assumed by it in this Agreement are legal and valid obligations binding on it in accordance with the terms hereof;
- (3) it has obtained any necessary governmental permission, licenses, authorization or clearances, if any, to execute this Agreement.

### 4. TERM

Unless sooner terminated pursuant to other provisions of this Agreement, the term of this Agreement shall be five (5) years commencing on the date hereof. This Agreement shall be subject to automatic extension for additional two (2) year periods unless either party, with or without cause, shall give written notice of termination to the other not less than ninety (90) days prior to the end of the initial term of this Agreement or any extension thereof.

### 5. MISCELLANEOUS

- (1) This Agreement shall be governed by UNIDROIT Principles of International Commercial Contracts (1994 version).
- (2) Neither party shall be liable to fulfill its obligations hereunder, or for delays in performance, due to causes beyond its reasonable control, including, but not limited to, acts of God, acts or omissions of civil or military authority, fires, strikes, floods, epidemics, riots or acts of war.
- (3) This Agreement sets forth the entire agreement between the parties hereto with respect to the subject matter hereof and is intended to supersede all prior negotiations, understandings and agreements. No provision of this Agreement may be waived or amended, except by a writing signed by the parties hereto.
- (4) This Agreement may be executed in one or more counterparts, each of which shall be deemed an original and together which shall constitute one and the same instrument.
- (5) The failure of either party to exercise any right or remedy provided for herein shall not be deemed a waiver of any right or remedy hereunder.
- (6) Any dispute, controversy or difference arising out of or in relation to or in connection

with this Agreement or for the breach thereof, shall be settled by arbitration in Tokyo, Japan, pursuant to the UNCITRAL Arbitration Rules and by three (3) arbitrators. The arbitration award shall be final and binding on both parties.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement on the date first set forth above.

Red Industries, Co.

Blue Electronics, Inc.

EXHIBIT 1

ORDER FORM

Pursuant to the Supply Agreement, Buyer hereby orders the following Product(s).

Product Number:

Quantity:

Delivery Date:

Blue Electronics, Inc.

---

## EXHIBIT 2

### List of Products

- |               |                        |
|---------------|------------------------|
| 1. PR-3 (LSI) | Unit Price 10,000 Arb. |
| 2. YR-5 (LSI) | Unit Price 10,000 Arb. |

## JOINT DEVELOPMENT AGREEMENT

THIS AGREEMENT made as of the 1st day of September, 2005, by and between Yellow Phone Ltd., a corporation organized and existing under the laws of Arbitria (hereinafter "Yellow"), and Blue Electronics, Inc., a corporation organized and existing under the laws of Arbitria (hereinafter "Blue")

WHEREAS, Yellow and Blue wish to co-operate with each other and jointly develop a product set forth below in such manner as mutually agreed:

NOW THEREFORE, in consideration of the mutual promises contained herein, the Parties agree as follows:

### ARTICLE 1 DEFINITIONS

(1) "Background IPR" means any Intellectual Property Rights of a party conceived, created, developed, or reduced to practice prior to, or independently of, any work performed pursuant to this Agreement.

(2) "Background Technology" means any technology of a Party conceived, created, developed, or reduced to practice prior to, or independently of, any work performed pursuant to this Agreement.

(3) "Confidential Information" means any business, marketing, technical, scientific or other information disclosed by any party which, at the time of disclosure, is designated as confidential or proprietary (or like designation), is disclosed in circumstances of confidence, or would be understood by the parties, exercising reasonable business judgment, to be confidential. Confidential Information includes, without limitation, all Background IPR, Background Technology, and the terms and conditions of this Agreement.

(4) "Intellectual Property Rights" or "IPR" shall mean all intellectual property rights, including without limitation, any rights in any invention, patent, discovery, improvement, know-how, utility model, trade-mark, copyright, industrial design or mask work, integrated circuit topography, trade secret and all rights of whatsoever nature in computer software and data, Confidential Information, and all intangible rights or privileges of a nature similar to any of the foregoing, including in every case in any part of the world and whether or not registered, and shall include all rights in any applications and granted registrations for any of the foregoing.

(5) "Joint IPR" means the Intellectual Property Rights mutually identified by the parties in this project as Joint IPR and conceived, created, developed, or reduced to practice in this

project pursuant to this Agreement.

(6) "Joint Technology" means the technology mutually identified by the parties in this project as Joint Technology and conceived, created, developed or reduced to practice in this project pursuant to this Agreement.

(7) "Party" means Yellow or Blue.

(8) "Parties" means Yellow and Blue.

ARTICLE 2 PROJECT

(1) The Parties will jointly develop such mobile phones that have the capability as mutually agreed upon between the Parties.

(2) Each Party will provide corresponding expertise to the other Party for the joint development of the mobile phones under this Agreement.

(3) All costs required for the development of the mobile phones shall be born equally.

. . .

ARTICLE 10 INTELLECTUAL PROPERTY

(1) Each Party shall retain all right, title, and interest in and to such Party's Background IPR and Background Technology.

(2) Each Party shall retain ownership of all right, title and interest in and to any IPR and technology developments it creates other than IPR and technology which have been identified to be Joint IPR and Joint Technology according to this Agreement.

(3) Joint IPR and Joint Technology shall be identified in Annex 1 as agreed between the Parties.

(4) The Parties agree that all Joint IPR and Joint Technology shall belong jointly to both Parties.

(5) Both Parties shall mutually agree upon the filing of applications and execution and delivery of any further documents that may be required in order to secure intellectual property rights, including but not limited to patent and copyright, in the Joint IPR and Joint Technology.

(6) While either Party may have the responsibility to file, prosecute and/or maintain patents, the filing, prosecuting or maintaining of such patents shall be at the sole discretion and judgment of that Party, and neither Party, nor their employees, agents or officers, shall have any responsibility or liability to the other party for any failure, mistake or error in the filing, prosecuting or maintaining of such patents.

. . .



ARTICLE 16 CONFIDENTIALITY

- (1) Each Party agrees, in the event it receives Confidential Information from the other Party, to take all reasonable actions to protect and hold such information in confidence in order to prevent its disclosure to third parties, to use such Confidential Information only for those purposes contemplated under this Agreement, and to disclose Confidential Information only to its employees on a need-to-know basis.
- (2) At all times during the term of the Agreement, each Party shall perform all reasonably required security procedures at its facilities and in connection with its business activities in order to protect the Confidential Information of the other Party, including but not limited to, controlled access to such Party's facilities and/or installations, use of security badges by its employees, contractors and others while on the premises or installation sites, and confidentiality agreements with its employees and contractors and such other security standards and procedures as shall be reasonably necessary to ensure the protection and non-disclosure of Confidential Information.
- (3) The obligations of each Party under this Article shall survive for three (3) years after the expiration or termination of this Agreement. Notwithstanding the foregoing, neither Party shall be required to protect or hold in confidence any information which:
  - a) is or becomes available to the public or to industry without the fault of the recipient;
  - b) is subsequently rightfully received by the recipient from a third party without obligation of restriction on further disclosure; or
  - c) is independently developed by the recipient as evidenced by its business records.
- (4) In case of any breach of any obligation under this clause, the Party who breaches such obligation shall pay 500,000,000 Arb upon the written request from the other Party, as liquidated damages.

ARTICLE 17 GOVERNING LAW

All questions arising out of or under this Agreement shall be governed by and construed in accordance with UNIDROIT Principles of International Commercial Contracts (1994 version).

. . .

## AGREEMENT

THIS AGREEMENT, made as of the 1st day of November, 2005 by and between Red Industries, Co., a corporation organized and existing under the laws of Negoland (hereinafter called "Red") and Blue Electronics, Inc., a corporation organized and existing under the laws of Arbitria (hereinafter called "Blue").

WHEREAS, Blue and Yellow Phone Ltd. agreed to develop a new mobile phone under the agreement dated September 1, 2005, a copy of which has been delivered to Red;

WHEREAS, Blue needs to develop a new LSI for the new mobile phone;

WHEREAS, Blue and Red wish to co-operate with each other and jointly develop a new LSI in such manner as mutually agreed:

NOW THEREFORE, in consideration of the mutual promises contained herein, the Parties agree as follows:

### ARTICLE 1 DEFINITIONS

(1) "Background IPR" means any Intellectual Property Rights of a party conceived, created, developed, or reduced to practice prior to, or independently of, any work performed pursuant to this Agreement.

(2) "Background Technology" means any technology of a Party conceived, created, developed, or reduced to practice prior to, or independently of, any work performed pursuant to this Agreement.

(3) "Confidential Information" means any business, marketing, technical, scientific or other information disclosed by any party which, at the time of disclosure, is designated as confidential or proprietary (or like designation), is disclosed in circumstances of confidence, or would be understood by the parties, exercising reasonable business judgment, to be confidential. Confidential Information includes, without limitation, all Background IPR, Background Technology, and the terms and conditions of this Agreement.

(4) "Intellectual Property Rights" or "IPR" shall mean all intellectual property rights, including without limitation, any rights in any invention, patent, discovery, improvement, know-how, utility model, trade-mark, copyright, industrial design or mask work, integrated circuit topography, trade secret and all rights of whatsoever nature in computer software and data, Confidential Information, and all intangible rights or privileges of a nature similar to any of the foregoing, including in every case in any part of the world and whether or not registered, and shall include all rights in any applications and granted registrations for any of

the foregoing.

(5) "Joint IPR" means the Intellectual Property Rights mutually identified by the parties in this project as Joint IPR and conceived, created, developed, or reduced to practice in this project pursuant to this Agreement.

(6) "Joint Technology" means the technology mutually identified by the parties in this project as Joint Technology and conceived, created, developed or reduced to practice in this project pursuant to this Agreement.

(7) "Party" means Red or Blue.

(8) "Parties" means Red and Blue.

## ARTICLE 2 JOINT WORKS

(1) Red and Blue will jointly develop a new LSI (the "Product") with the capability to be mutually agreed between the Parties.

(2) Red and Blue will provide corresponding expertise to the other Party for the joint development of the Product.

(3) Red will appoint a project leader who will manage the project to develop the Product.

(4) Blue will send a competent person who will be a project sub-leader of the project.

(5) The project leader and sub-leader will cooperate to manage the project.

. . .

## ARTICLE 10 INTELLECTUAL PROPERTY

. . .

(1) Each party shall retain all right, title, and interest in and to such party's Background IPR and Background Technology.

(2) Each Party shall retain ownership of all right, title and interest in and to any IPR and technology developments it creates other than IPR and technology which have been identified to be Joint IPR and Joint Technology according to this Agreement.

(3) Joint IPR and Joint Technology shall be identified in Annex 1 as agreed between the Parties.

(4) The Parties agree that all Joint IPR and Joint Technology shall belong jointly to both Parties.

(5) Both Parties shall mutually agree upon the filing of applications and execution and delivery of any further documents that may be required in order to secure intellectual property rights, including but not limited to patent and copyright, in the Joint IPR and Joint Technology.

(6) While either Party may have the responsibility to file, prosecute and/or maintain patents, the filing, prosecuting or maintaining of such patents shall be at the sole discretion and judgment of that Party, and neither Party, nor their employees, agents or officers, shall

have any responsibility or liability to the other party for any failure, mistake or error in the filing, prosecuting or maintaining of such patents.

. . .

#### ARTICLE 16 CONFIDENTIALITY

- (1) Each Party agrees, in the event it receives Confidential Information from the other Party, to take all reasonable actions to protect and hold such information in confidence in order to prevent its disclosure to third parties, to use such Confidential Information only for those purposes contemplated under this Agreement, and to disclose Confidential Information only to its employees on a need-to-know basis.
- (2) At all times during the term of the Agreement, each Party shall perform all reasonably required security procedures at its facilities and in connection with its business activities in order to protect the Confidential Information of the other Party, including but not limited to, controlled access to such Party's facilities and/or installations, use of security badges by its employees, contractors and others while on the premises or installation sites, and confidentiality agreements with its employees and contractors and such other security standards and procedures as shall be reasonably necessary to ensure the protection and non-disclosure of Confidential Information.
- (3) The obligations of each Party under this Article shall survive for three (3) years after the expiration or termination of this Agreement. Notwithstanding the foregoing, neither Party shall be required to protect or hold in confidence any information which:
  - a) is or becomes available to the public or to industry without the fault of the recipient;
  - b) is subsequently rightfully received by the recipient from a third party without obligation of restriction on further disclosure; or
  - c) is independently developed by the recipient as evidenced by its business records.

#### ARTICLE 17 GOVERNING LAW

All questions arising out of or under this Agreement shall be governed by and construed in accordance with UNIDROIT Principles of International Commercial Contracts (1994 version).

. . .

## Employee Secondment Agreement

Blue Electronics, Inc. (hereinafter “Blue”) and Red Industries, Co. (hereinafter “Red”) agree to execute this agreement with respect to work conditions and the bearing of expenses, etc. concerning the employee seconded from Blue to Red (hereinafter the “Seconded Employee”).

Article 1 Blue shall place the Seconded Employee in Red, and have the Seconded Employee undertake the job duty as an assistant leader concerning the development of LSI under the direction and in the location of Red, pursuant to the agreement dated November 1, 2005.

Article 2 The Seconded Employee shall be ○○○○.

Article 3 The secondment period of the Seconded Employee from Blue to Red shall be from November 1, 2005, until December 31, 2007.

Article 4 Blue shall put the Seconded Employee on leave of absence during the secondment period mentioned above, and shall send the Seconded Employee on loan as an employee of Red. The Seconded Employee shall promptly return to work at Blue when this Agreement is terminated or rescinded.

Article 5 The Seconded Employee shall follow the office regulations of Red.  
( However, this excludes annual paid holidays, benefit package and severance pay)

2. With regard to annual paid holidays, benefit package and severance pay, the regulations of Blue shall be applied.

Article 6 With regards to the pay and bonuses of the Seconded Employee, Blue shall pay such items directly to the Seconded Employee under the regulations of Blue, and Blue shall demand from Red all the amounts of basic salary and other benefits.

Article 7 The Seconded Employee shall continue to be enrolled in health insurance, employee’s pension insurance and employment insurance through Blue, and Blue shall bear the employer’s contributions therefor.

2. Worker’s accident compensation insurance for the Seconded Employee shall be covered by Red, and any premiums concerning this shall be borne by Red.

Article 8 Various expenses which may arise in connection with the work commanded by Red, such as business trip expenses, shall be paid directly to the Seconded Employee by Red pursuant to the regulations of Red.

- 2. Necessary costs for commuting shall be paid directly to the Seconded Employee by Blue pursuant to the regulations of Blue.

Article 9 Matters not provided for in this Agreement or questions which may arise with respect to the provisions of this Agreement shall be resolved through consultation between Blue and Red.

Article 10 The effective period of this Agreement shall be from the date of execution of this Agreement until the last day of the secondment period. However, when the purpose in Article 1 of this Agreement is achieved, this Agreement shall terminate as of that point in time.

Article 11 Even during the period of this Agreement, this Agreement may be rescinded if Blue or Red notifies the other party in writing at least one month before the desired date of cancellation.

Blue Inc.

---

Red Co.

---

< Attachment 10 >

September 6, 2006

Red Co.

Blue Inc.

GM of the Mobile Phone Business Department

Greetings.

As per the Attachment, please send 30,000 units of MODEL PR-3 immediately. However, please note that sending the order form in the Attachment does not indicate that we withdraw the claim that the agreement for 30,000 units of MODEL PR-3 had been executed between your company and our company as of August 21<sup>st</sup>.

Sincerely yours,

< Attachment 11 >

September 7, 2006

Blue Inc.

Red Co.

GM of the Sales Department

Greetings.

Thank you for your correspondence.

Our company understands that the agreement for 30,000 units of MODEL YR-5 had been executed between your company and ours as of August 21<sup>st</sup>. It does not seem appropriate to receive orders from your company while we still have a difference in mutual understanding on this point. We believe it is best if you withdraw the order from the other day for the time being, and that we have a separate consultation.

With regards,



Strictly Confidential

Memorandum

\*The matters listed in the basic framework column are matters as to which agreement has almost been reached in the meetings so far.

\*The matters listed as debated issues are matters as to which agreement has not been reached because there was not sufficient time to fully discuss them, although opinions were voiced in the meetings so far.

1. Concerning the business transfer of the Integrated Circuit Department

(1) Basic framework

- Red Co. is to assign the Integrated Circuit Department to Blue Inc., and Blue Inc. is to receive assignment of the same.
- As a result of this assignment, the assets and liabilities of Red Co. with respect to the Integrated Circuit Department are to be transferred to Blue Inc.
- After executing a letter of intent pursuant to this proposal, due diligence will be carried out for three months with respect to the Integrated Circuit Department.

(2) Issues

\* Matters which Blue Inc. has suggested to be included as conditions for adopting this proposal

- After the assignment, Red Co. will not engage in the integrated circuit business.
- In the event there is a significant defect in the assigned assets, Red Co. will compensate for the loss that Blue Inc. suffers as a result of such defect.

\* Matters which Red Co. has suggested to be included as conditions for adopting this proposal

- Blue Inc. will not lay off, for two years after the assignment, the employees of the Integrated Circuit Department who are transferred to it as a result of the assignment.
- The standards for work environment and social insurance will not be lowered from what is being provided currently.

\* Assignment price: Blue Inc. has suggested as the appropriate price 2 billion US dollars for the asset value and 2 billion US dollars for the goodwill, resulting in the total amount of about 4 billion US dollars. (Red Co. is examining the adequacy of this price).

2. Concerning the establishment of a joint venture company

(1) Basic framework

- Red Co. and Blue Inc. will establish a joint venture company which will carry out research, development and manufacturing in relation to the latest model mobile phones based on 50:50 investment (in the range of 2 billion US dollars for each company), either in Negoland or in Arbitria.
- The board of directors will consist of four members, and Red Co. and Blue Inc. will select two members each.
- Red Co. and Blue Inc. will each dispatch to the joint venture company the necessary staff for smooth and effective performance of the joint venture business.
- Red Co. and Blue Inc. will each license to the joint venture company the necessary technologies and know-how for smooth and effective performance of the joint venture business.

(2) Issues

- President: Red Co.'s assertion: to be selected from Red Co.; Blue Inc.'s assertion: to be selected from Blue Inc.
- Company name: Red Co.'s assertion: Red & Blue, Co.; Blue Inc.'s assertion: Blue & Red Inc.
- Scope of business: Blue Inc.'s assertion: to be limited to mobile phones sold in Arbitria; Red Co.'s assertion: without limiting the destination countries for the sales, to seek the development and manufacture of mobile phones that would be widely accepted in international markets.

3. Concerning the execution of a long-term cooperation agreement

(1) Basic framework

- Both Red Co. and Blue Inc. will carry out research and development with respect to mobile phones in collaboration.
- The basic research and development policies will be determined by a joint committee of four members, with two members each to be selected by Red Co. and Blue Inc.
- Red Co. and Blue Inc. will jointly hold the rights with respect to the technologies and know-how that have been researched and developed jointly, and will split equally any profits realized from those technologies and know-how.
- The annual research and development budget will be about 3 billion US dollars.

(2) Issues

\* Matters which Blue Inc. has suggested to be included as conditions for adopting this proposal

- The person responsible for research and development shall be selected from among Blue Inc.'s research staff.

\* Matters which Red Co. has suggested to be included as conditions for adopting this proposal

- In return for provision of the research facility by Red Co., the development funds will be borne by Blue Inc. and Red Co. in the proportion of seven to three, respectively.

