

## **Tooling Proposal - DISCUSSION BRIEF**

**SUBJECT: TOOLING PROPOSAL: ENSURE “TRICKLE DOWN” OF GOVERNMENT LOANS PROCEEDS TO DETROIT 3 OCCURS TO REACH TOOLING INDUSTRY.**

Following is a brief outline which was developed to provide you with an overview of the issues facing the Tool, Die, & Mold (TDM) industry in the United States, as well as what we believe presents a viable solution: [Note: Canada is already well underway with a similar proposal for Canadian Government loans to Detroit 3.]

### **THE GOALS and EMPLOYMENT BENEFITS**

1. Prevent avoidable bankruptcies in TDM sector;
2. Protect and stimulate employment;
3. Enhance liquidity for TDM sector companies (without the need for banks to amend existing bank credit facilities);
4. Mitigate the risk of bad debts which erode company profitability, productivity and access to credit;
5. Ensure a mechanism for “trickle-down” for direct loans proposed by Government to the OEMs to companies throughout the supply chain;
6. Ensure the TDM Sector is properly recognized as a critical supplier in any loan agreements or bankruptcy styled restructuring of the subject vehicle manufacturer;
7. Reduce the risk of taxpayers paying twice for the bailout: once at advancing of loan proceeds to vehicle manufacturer, and a second time when tooling proceeds from the vehicle manufacturer are diverted by the “Middleman” (the Tier 1 parts manufacturer) prior to delivery of funds to the tool source, resulting a bad debt forcing tools source to lay off employees or file Chapter 11

### **THE ISSUES**

1. Vehicle Manufacturers (OEM) driven payment terms for tooling, which result in a delay of their payment obligations, actually increases the acquisition cost of tooling and vehicle production costs, and has stretched payments to Tool, Die, & Mold (TDM) manufacturers by up to 24 months from award of contract and beyond. These OEM driven payment terms have resulted in:
  - a) In excess of \$3 billion in completed tooling fabricated by US tool sources for parts manufacturers waiting for OEMs to make payments to Tier 1 parts companies, who in turn pay the tool source – payment obligations which are not recorded in the books of the OEM;
  - b) Payments to tool sources for completed tooling increasing 5-18 months after delivery of the tooling to the Tier1 parts company;
  - c) OEMs, at their sole discretion, can delay vehicle programs indefinitely without the requirement to pay for the tooling completed to date NOR pay any additional compensation for the delayed tooling eg. Interest and carrying costs;
  - d) Parts manufacturers who sell directly to the OEM (Tier 1 supplier) are dictating tooling payment terms such as “TDM is paid only after Tier 1 is paid”, implying that if the Tier 1 never gets paid by the OEM (e.g. bankruptcy), then the TDM has no claim to payment from the Tier 1; and
  - e) Certain Tier 1 parts manufacturers are requiring TDM manufacturers waive their statutory lien rights provided for under the Michigan Mold Lien Act and the Michigan Special Tools Lien Act in order to obtain a purchase order, thereby relieving the Tier 1 of any payment obligation for the tooling in the event of a bankruptcy filing by the Tier 1.

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NO OTHER sector in the automotive industry has to wait more than 60 days for payment after delivery of goods. Parts suppliers are paid on average 45 days after parts delivery. The OEM is paid within 5 days of vehicle delivery to the dealership. Tool sources are waiting 5-18 months or more post delivery for payment.

2. Banks generally: dislike lending against work-in-progress and single purpose assets; and have a 90-120 day cut-off for accepting accounts receivable as collateral for lending purposes. When these traits of the tooling sector are coupled with the present economic and liquidity environment the results are: a) the closure of a large number of TDM suppliers along with the loss of employment opportunities; b) increased stress on the financial covenants with banks for remaining TDM suppliers; c) Access to working capital financing, and the required flexibility in financial covenants, to support tooling operations is severely limited and in many cases impossible to obtain;
3. Many new tooling opportunities exist today, which are available for US suppliers to bid on and to win. Tooling is the leading edge indicator of the industry cycle and automotive economic recovery. However, a lack of access to working capital, COUPLED WITH a risk profile which is simply TOO HIGH with the potential for payment receipts out 24 months, will have many of these shops, who are capable of winning this work, sitting on the sidelines and thereby laying off employees.

### **THE SOLUTION**

**The tooling sector is not requesting any form of “bail out”.** We are seeking: a reduction in OEM driven payment terms commensurate with the risk profile of the present industry, AND to ensure these funds “trickle down” and make it through the cash strapped Tier 1 parts manufacturers, who act as Middlemen for tooling proceeds, to the Tool Source. As such we are requesting that:

1. Conditions be attached to the OEM loan package that the Government is currently considering to assist the automotive industry, which ensure that the Tier I & Tier II supply base receives some of the benefit;
2. Loan conditions would provide that the OEM (recipient of the Government financing) be required to provide PROGRESS DRAWS at predetermined project milestones where production tooling is sourced with a US tool supplier who manufactures the tool in US [NOTE: A draft sample of the required legal wording for insertion into the Loan Agreements is available for review] or, at the very least pay 90% of the cost of tooling to the Tier 2 at delivery of tooling to the Tier 1, with 10% held back until PPAP has been completed;
3. While government loans are outstanding under the proposed aid package, the OEMs would be required to complete payment for tooling:
  - a) Upon completion of successful buy-off in the Tier 1 manufacturer’s facility (versus the current practice of payment at Production Part Approval Process – “PPAP”- or Start of Production – “SOP”), thereby accelerating final payment by 5-18 months;
  - b) Immediately, if they cancel a program; and
  - c) Immediately, if they delay a program longer than 90 days.
4. Ensuring that the OEM releases tooling funds at an appropriate interval will not fully remedy the risk to the tool source, as these funds must then navigate through the cash strapped Tier 1 parts companies. [eg. Collins & Aikman, Cadence and Plastech are high profile Tier 1 bankruptcy examples where the tooling funds the OEMs disbursed to the Tier 1 did not make it through to the tool sources.] As such, an oversight mechanism/structure must accompany the above in order to safeguard government loan funds, OEMs as the borrowers of these

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funds, and the tool sources as the ultimate recipient of these funds. [Tooling & Equipment Capital Solutions Inc. has structured a Bankruptcy Remote Trust mechanism for the US.]

### **THE BENEFIT TO THE INDUSTRY**

1. The contract cycle for the large number of US tool, die and mold sources will be shortened by 25-50%, immediately improving the liquidity, improving their financial ratios – which are presently under stress, and alleviating significant bank pressure [Note: Before and After Balance Sheet example is available for review];
2. Tool, Die, & Mold manufacturers will have access to much needed cash flow to support in-progress and future tooling projects, since they will receive payments for tooling projects in a far more timely manner– a practice that will substantially reduce contract cycle time;
3. Because of the immediate improvement in financial condition brought on by accelerating payments, and the far greater certainty of timely payments arising from the proposed Trust structure, banks will develop an increased appetite for providing financing to tooling producers because of enhanced liquidity and more certain cash flow;
4. The Tier 1 parts manufacturers will also benefit from this proposal, since they too would receive cash flow related to project capital in addition to tooling, such as assembly equipment and production fixtures, and the proposal reduces their down stream risk to supplier collapse at the Tier II level; and
5. The government greatly reduces the likelihood of having to pay twice for this economic situation: The first time on the OEM bail out. The second time when taxpaying US TDM companies, who have extended unduly long credit – not of their own volition but out of necessity to be awarded business - write-off bad debts to the OEMs and Tier 1's.

Furthermore, under the proposed structure the Government loans to the OEMs will have direct, traceable, attribution to several hundred Tool, Die & Mold manufacturers, located throughout the US, many of whom are small and medium sized entities, and not just simply one or three OEMs.

### **ECONOMIC PERSPECTIVE**

Michigan alone has 1200 mold and die shops that produce tooling for the automotive industry and employ 17,000 with annual sales of \$2.6 billion.

The balance of the Automotive focussed US tool, die and mold industry – largely located in Ohio, Indiana, Illinois, Kentucky and Alabama – in aggregate would be similar or greater than that of Michigan.