

# Agency and distributorship agreements

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## 1. Introduction

This booklet summarises the main points to consider when negotiating an agency or distributorship agreement. It is a guide to the principal items to be dealt with in an agreement between a supplier and his local agent or distributor. Not every point in this booklet will be relevant in all circumstances, nor are the checklists an exhaustive list of all matters that may apply in a particular case. As such, this booklet is not a substitute for specialist legal advice on a specific transaction or on the drafting of the agreement itself.

## 2. Agent versus distributor

Although the terms “agent” and “distributor” are used interchangeably in the commercial world, there is a distinct legal difference between the two. In strict legal terms, an agent is simply someone who acts on behalf of another in assuming contractual obligations on that other's behalf. Whilst the function of a distributor is to re-sell goods bought from a supplier, an agent's function is to provide a service to the supplier, either introducing customers to the supplier, or concluding contracts on the supplier's behalf. Depending on the circumstances of the particular case:

- the agent may have authority to enter into contracts on behalf of the supplier;
- the contract for the sale of the products or supply of services will be between the supplier and the customer, with the agent acting as intermediary, the supplier controlling the price and other terms of supply to the customer;
- the agent will generally have no liability under the contract made on the supplier's behalf;
- the supplier, not the agent, will bear the risk of bad debts; and
- the agent will usually be remunerated by commission paid by the supplier.

Under a distributorship agreement, on the other hand, the distributor purchases goods from the supplier and resells them on his own account. Accordingly:

- the distributor has no authority to bind (i.e. incur contractual obligations on behalf of the supplier);
- because there are two separate contracts for the sale of the products:
- from the supplier to the distributor
- from the distributor to the customer

the supplier has no direct contractual link with the customer and (depending on the territory concerned) the supplier may be prohibited from controlling the distributor's resale prices;

- the distributor bears the risk of customers' bad debts (and the supplier's risk of bad debts is channelled into one debtor, i.e., the distributor); and
- the distributor is remunerated from the profit on the supply of the products to the customer.

The supplier should decide at the outset what form of legal relationship would best suit his business.

Generally, where the supplier is exporting, he will prefer to have a distributor in close touch with the market and the credit-worthiness of customers. The supplier may find it easier to deal with one known entity (the distributor) rather than perhaps many unknowns (customers). It may also be that the law of the place of performance of the agreement or of the agent's residence would entitle an agent (but not a distributor) to compensation for termination of the agreement even if the parties try to exclude this right. For example, this is the position in Great Britain for many agents under the Commercial Agents (Council Directive) Regulations 1993 (as amended) (“the Regulations”).

In other circumstances, there may be commercial reasons why the supplier would prefer to appoint an agent.

On 1 January 1994 the Regulations came into effect implementing a 1986 European Directive which attempted to harmonize the laws of member states relating to self-employed commercial agents.

The Regulations represent substantial changes to the English law of agency. The terms of the regulations are implied into commercial agency agreements, both written and oral, formal and informal.

For a more detailed consideration of the effects and implications of the regulations please refer to our practical booklet entitled The Commercial Agents Regulations.

Whichever solution is adopted, one of the most important legal considerations underlying an agency or distributorship agreement of any economic significance is likely to be in the area of competition law - both UK and EC.

### **3. Competition law**

#### **3.1. UK competition law**

The Competition Act 1998, which came into force in March 2000, introduced a new regulatory regime within the United Kingdom. The Act prohibits all agreements between undertakings, decisions by associations of undertakings or concerted parties, which may affect trade within the UK or which have as their object or effect the prevention, restriction or distortion of competition within the UK.

Anti-competitive behaviour or arrangements in whatever form - written, unwritten, formal or informal – are caught. Moreover, whether an agreement is deemed anticompetitive, is to be judged on its effect, not its wording or form.

An agreement falls under the prohibition only if it has an “appreciable” effect on competition within the UK. In general an agreement will have no appreciable effect on competition if the parties’ combined share of the relevant market does not exceed 25 per cent. Exceptions to this are agreements which directly or indirectly fix prices, impose minimum resale prices, or share markets. Such agreements will be judged by the OFT as having an appreciable effect on competition (even where the parties’ combined market share is less than 25 per cent.)

Certain categories of agreement are specifically excluded from this prohibition. These categories include vertical agreements – agreements between businesses operating at different levels of the chain, for example supplier and distributor, principal and agent.

#### **3.2. European competition law**

In addition, close attention will have to be given to European competition rules when considering an arrangement that covers all or any part of the common market.

Article 81(1) of the EC Treaty prohibits agreements between independent undertakings which may affect trade between Member States of the EU and which have as their object or effect the prevention, restriction or distortion of competition within the common market.

Agreements which contravene Article 81(1) are automatically void - at least in respect of their “anti-competitive” provisions - unless they have been “notified” to and “exempted” by the European Commission in Brussels. Notification is a cumbersome process and the Commission adopts very few formal decisions of exemption each year. Broadly speaking, the criterion for exemption is that the economic benefits of an agreement outweigh its restrictive effects.

In 1999, the Commission made a new Regulation exempting from Article 81(1) various categories of agreements between businesses operating at different levels of the production or distribution chain. For example, supplier and distributor. This is an automatic exemption; it is not necessary to notify the agreement in order to obtain an individual exemption.

The Regulation sets out a list of hardcore restrictions which exclude the whole agreement from the scope of application of the exemption. However, a restriction is not classified as hardcore if it is on active sales into the exclusive territory or to an exclusive customer group reserved by the supplier or allocated by the supplier to another buyer, where such a restriction does not limit sales by the customers of the buyer.

Attempts by manufacturers of goods to protect their distributors against competition from parallel imports have been repeatedly condemned by the European Commission and can lead to the imposition of heavy fines. A further point to bear in mind is that whilst in certain cases the imposition of restrictions against competition on an exclusive distributor can be regarded as an acceptable quid pro quo for the grant of exclusive rights it is more difficult to justify such restrictions where the distributor is simply given non-exclusive rights.

Special rules apply where a manufacturer proposes to set up a network of distributors.

## **4. The agreement**

Whether the appointment is of an agent or a distributor, the form of agreement between the supplier on the one hand and the agent or distributor on the other hand defines the parties' relationship and sets out the ground rules for the future.

The agreement should also determine the rights and obligations of both sides if the relationship goes wrong.

In part 5 and 6 of this booklet are brief notes on the principal points that should be covered in first, an agency agreement, and secondly, a distributorship agreement. To a large extent, the two types of agreement are similar to each other, although they reflect different legal relationships.

## **5. Agency agreements checklist**

### **5.1. Parties**

- state clearly the identity of the parties. If a company, state the place of incorporation, registered/principal office and any registered number
- are the obligations of the agent to be guaranteed?

### **5.2. Definitions**

- the Territory covered by the Agreement
- the products/services which are the subject of the Agreement
- minimum targets to be attained

### **5.3. Scope of the appointment**

- is the agent exclusive/sole/non-exclusive?

### **5.4. Duration of the Agreement**

- fixed period
- any initial minimum period
- right to renew/automatic renewal
- right to terminate by notice
- length of notice period

### **5.5. Responsibilities of the agent**

- to promote sales
- not actively to market outside the "Territory"
- not to deal in/be concerned with competing products/services
- to sell at specified prices
- not to give unauthorised warranties or representations
- not to bind the supplier to give credit
- to maintain offices and other facilities (for sales, service, repair, parts, etc.)
- to pass back to the supplier market information and to provide reports and returns
- to keep accounts and records, and allow the supplier to inspect and audit
- to maintain separate accounts

- to refer to the supplier enquiries from outside the “Territory”
- to inform the supplier of disputes with customers
- not to assign the agency
- not to sub-contract/delegate fulfilment of contractual obligations
- not to incur any liability on behalf of the supplier, save with prior written consent
- to indicate in dealings that the agent acts as agent for the supplier
- to defray expenses associated with the agency
- to keep confidential any secret “know-how” disclosed to the agent
- to supply customers with Principal’s standard terms and conditions.

#### **5.6. Responsibilities of the supplier**

- to supply promotional literature and/or samples
- to provide advice and assistance
- to refer to the agent enquiries from within the “Territory”, where practicable

#### **5.7. Supply of products/services**

- manner in which orders are to be transmitted to supplier
- supplier not obliged to accept any order
- agent to offer products/services only on supplier’s conditions of sale
- agent to carry out credit risk evaluation of customers

#### **5.8. Commission**

- basis of commission/remuneration
- time, manner and place of payment
- currency of payment
- withholding tax

#### **5.9. Intellectual property rights (patents, trade marks, etc)**

- agent not to use the intellectual property rights of the supplier without consent
- agent to notify supplier of unauthorised third party use of intellectual property rights and assist in infringement proceedings
- agent to cease to use on termination of the agreement any intellectual property rights for which consent was given

#### **5.10. Reservations of the supplier**

#### **5.11. The supplier’s right to terminate the Agreement**

- on breach by the agent
- on insolvency of the agent
- on change in control of the agent
- on agent being prevented from performing its duty
- on failure to achieve sales targets
- on purported assignment by the agent
- if the agreement becomes illegal

#### **5.12. Consequences of termination**

- commission entitlements of agent on termination
- obligations of agent on termination
- rights and liabilities of the parties to survive termination
- no compensation for the agent on termination
- return of promotional literature, samples and any stocks
- indemnity or compensation under the Regulations

**5.13. Choice of law, submission to the jurisdiction and address for service**

**5.14. Whole agreement provision**

**5.15. No joint venture or partnership**

**5.16. General provisions**

**6. Distributorship agreements checklist**

**6.1. Parties**

- state clearly the identity of the parties. If a company, state the place of incorporation, registered/principal office and any registered number
- are the obligations of the distributor to be guaranteed?

**6.2. Definition**

- the Territory covered by the Agreement
- the products the subject of the Agreement
- any trade marks involved

**6.3. Scope of Appointment**

- is the distributorship exclusive/sole/non-exclusive?

**6.4. Duration of the Agreement**

- any initial minimum period
- right to renew/automatic renewal
- right to terminate by notice

**6.5. Terms of sale of products from supplier to distributor**

- supplier's right to refuse orders
- prices, provisions for fixing prices, provisions in the event of failure to fix prices
- pricing provisions on resale (subject to local law)
- terms of payment/means of payment (e.g. letter of credit)
- distributor to purchase "products" only from the supplier
- supplier's conditions of sale to apply
- delivery terms (ex works, CIF, FOB, etc.)
- reservation of title
- warranties
- limitation of liability
- supplier's right to improve or modify the "products"
- distributor's obligation to purchase annual minimum quantities of "products" and consequences of failure (termination/change of scope of appointment)

**6.6. General obligations on distributor**

- to promote sales
- not to deal in competing products during the Agreement
- not outside the "Territory" and in relation to "products" to seek purchasers, establish any branch or maintain any distribution depot
- to maintain offices and other facilities (for sales, service, repair, parts, etc.)
- to pass back to the supplier market information and provide reports and returns
- to keep accounts and records, and allow the supplier to inspect and audit
- to comply with local laws
- not to alter or change "products" or packaging
- to conform to the supplier's marketing policies

- to keep sufficient stocks of the “products” and of parts
- to maintain sufficient qualified staff
- qualifications for appointment of local dealers

#### **6.7. Advertising**

- minimum advertising commitment on distributor
- form and content of advertising to be approved by supplier
- supplier to provide certain promotional literature free of charge

#### **6.8. Intellectual property rights**

- all rights to Trade Marks remain with supplier
- distributor not to endanger application for registration/ registration of Trade Marks
- control of prosecution/defence of infringement proceedings and sharing of spoils/liabilities

#### **6.9. Technical support and confidentiality**

- supplier to provide know-how, technical support and training
- obligation of confidentiality upon distributor in respect of know-how disclosed
- confidentiality obligation to continue after the termination of the Agreement

#### **6.10. Reservations of the supplier**

#### **6.11. The supplier's right to terminate the Agreement**

- on breach by the distributor
- on failure by the distributor to achieve sales targets
- on insolvency of the distributor
- on change in control of distributor
- on distributor's being prevented from performing its duty
- on distributor's failing to purchase minimum quantities
- on purported assignment by distributor
- if the agreement becomes illegal

#### **6.12. Consequences of termination**

- rights and liabilities of the parties to survive the termination
- resale of merchantable stocks to supplier
- destruction of all other stocks
- distributor to cease use of Trade Marks
- distributor to supply customer lists

#### **6.13. Choice of law, submission to the jurisdiction and address for service**

#### **6.14. Whole agreement provision**

#### **6.15. No joint venture or partnership**

#### **6.16. General provisions**

### **7. Fox Williams**

Fox Williams is an independent business law firm based in the City of London. We have a strong reputation for our core areas practice of corporate, employment, ecommerce and partnership law.

The firm's areas of specialisms include corporate, employment, dispute resolution, commerce & technology, property and partnership. Operating as business partners with our clients, we have built a solid reputation for advising on complex legal and regulatory issues in our core areas of expertise. A distinguishing feature of Fox Williams is that it is often first choice for referrals of work from other law firms when City expertise is required.



The firm's foundations are built upon an entrepreneurial spirit – which enables us to understand our clients aspirations, current needs and future requirements. We give clients a high degree of partner involvement, with the objective of delivering a fast and responsive service. At the same time, we strive to create a happy and efficient working environment for all members of the firm, which has resulted in an Investors in People accreditation.

We adopt a particular approach to our work, which involves making a special effort to understand the business needs of our clients, and delivering a fast, responsive service.