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3HR Legal Weekly

Commercial

Commercial Contracts: (2) Marketing agreements – agency, distribution and exclusivity

Agency and distribution agreements are the two most commonly encountered marketing agreements when commercial suppliers decide not to market goods themselves but appoint an intermediary instead. This can be for a number of reasons, such as lacking the resources they need to market the goods effectively or they may want to break into a new and unfamiliar market where they require the expertise of a third party.

Agency

A true sales agency agreement is one where the agent makes contracts with customers on behalf of its principal; the agent binds the principal, so there is a contract between the principal and the customer (but none between the agent and the customer). The principal is liable for the acts of his agent and that is one of the key reasons why care should be taken in drafting such agreements.

The agent does not hold normally stocks of the goods but it may have samples to show prospective customers. When the goods are sold, title to the goods passes direct from the principal to the customer. The agent never owns the goods, it is an intermediary and will not incur liability if the goods are defective.

Other types of agency agreement are possible, like 'introducing' agreements where the agent simply finds customers and introduces them to the principal, which then negotiates and makes the contract for itself. These agreements can also be used where the agent finds customers and negotiates terms on the principal's behalf but without having the authority to make the contract.

Distribution

In a distribution agreement, the supplier sells goods to the distributor, which buys them in order to re-sell on its own behalf.

The distributor owns the goods, which it sells, and title to the goods passes from the distributor to the customers. The supplier has no contractual relationship with the distributor's customers and so will have no contractual liability for the state of the goods. If the goods are defective, the supplier may, however, be liable to end users for product liability (for example, under the Consumer Protection Act). Again, great care should be taken when drafting such agreements.

Exclusivity

Whether the manufacturer decides to appoint an agent or a distributor, it will be important to decide the extent to which the agent/distributor will be protected from competition within the territory where it is operating. There are three options:

- Exclusive agency/distributorship: the manufacturer agrees not to appoint any other agents/distributors within the territory and will not sell the products within the territory itself.
- Sole agency/distributorship: the manufacturer agrees not to appoint any other agents/distributors within the territory, but remains free to sell the products within the territory itself.
- Non-exclusive agency/distributorship: the manufacturer can appoint other agents/distributors within the territory, and can sell the products within the territory itself.

The choice will depend on various factors, including the bargaining power of the parties. Exclusivity is preferable for the agent or distributor, and may be important to allow a new appointee to establish itself within a territory. Businesses often regard territorial exclusivity as a fundamental term, particularly in a distribution agreement, in order to benefit as much as possible from their initial investment. Without the grant of exclusivity, a potential distributor might not agree to take on the distributorship at all. Where exclusivity is granted, the manufacturer should put in place measures to ensure that the territory is fully exploited, such as minimum target obligations.

If you are thinking about entering into a marketing arrangement, either as the supplier or the agent/distributor, and would like to discuss the agreement with 3HR Legal beforehand, please do not hesitate to contact our Commercial team who will be able to assist you with both the drafting and review of the documents.

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