



## DISTRIBUTION OPTIONS

L. Donald Prutzman  
Tannenbaum Helpert Syracuse & Hirschtritt LLP,  
New York

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## Owned Outlets

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- **Simple, do-it-yourself**
- **Hire own employees, directly or through subsidiary**

## Sales Agents

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- **Hire local agent**
- **Agent:**
  - **Arranges sales, performs merchandising**
  - **Does not take title**
  - **Receives commission on sales**
- **Agent or supplier:**
  - **Advertises and markets**
  - **Fulfills sales**
  - **Bills and collects**

## Independent Distributors

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- Distributor buys from supplier
- Takes title and resells at profit

## Franchising

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- Essentially an independent distributor with specific elements:
  - License to use trademark in business name or products
  - Prescribed marketing plan or method of operation
  - Franchise fee
  - (Fee plus *either* of first two elements in NY)
- Disclosure/registration requirements
- Restrictions on termination, other aspects

## Joint Ventures

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- **Partial ownership of foreign distribution partner**
- **JV can be agent, distributor, franchise**

## Licensing Manufacturing Rights

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- **IP owner licenses manufacturer in target market**
  - Patent, copyright, trademark or trade secrets
- **Manufacturer makes goods, sells them at profit**
- **Licensor receives royalty**

## Private Label

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- **Reverse licensing: Target market retailer distributes under own brand**

## +/-: Costs & brand image control Owned outlets

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### Advantages

- **Maximum control**
  - Marketing
  - Presentation
  - Sales methods
  - Service
- **Retain all profits**

### Disadvantages

- **Bear all costs**
  - Start-up capital
  - Facilities and equipment
  - Employees
  - Administration and overhead
  - Collection risk
- **Jurisdiction for liability**
- **Taxation**
- **Regulatory compliance**
  - Foreign ownership restrictions
  - Qualify to do business
  - Employment laws
- **Less local knowledge?**

## +/-: Costs & brand image control Sales agents

### Advantages

- **Local knowledge**
  - Market conditions
  - Customs and culture
- **Agent bears local costs**
- **Avoid employment laws?**
  - Corporate agent with own EEs?
- **Options for allocating duties, costs**
  - Advertising and marketing
  - Delivery, billing, collection
    - Risk of loss could mean not a true agent
- **Control through contract**

### Disadvantages

- **Regulatory compliance**
  - Doing business through agent
- **Taxation?**
  - Where is sale made?
- **Employment laws?**
  - Could agent be deemed EE?
- **Cost of commissions**
- **Barriers to and costs associated with termination**

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## +/-: Costs & brand image control Independent Distributors

### Advantages

- **Local knowledge**
  - Market conditions
  - Customs and culture
- **Local costs borne by distributor**
- **Potential to avoid jurisdiction, taxation**
- **Option to retain or assign advertising and marketing role**

### Disadvantages

- **Give up distribution profit**
- **Some nations tax payments to foreign businesses**
- **Reduced control, except by contract**
- **Potential liabilities and costs of termination**
- **Possible protection to domestic distributors**

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## **+/-: Costs & brand image control Franchising**

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### **Advantages**

- **Similar to independent distributor advantages**
- **Franchise fee may provide working capital/income**
- **Control through marketing plan, contract**

### **Disadvantages**

- Give up some distribution profit (but franchise fees)
- Some nations tax payments to foreign businesses
- Regulatory compliance vs. lack of regulation
- Administrative costs to monitor franchisees
- Risk of poor performance

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## **+/-: Costs & brand image control Joint Ventures**

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### **Advantages**

- Same pluses as form used
- Added control through ownership, management rights

### **Disadvantages**

- Same minuses as form used
- Potential jurisdictional and tax exposure
- Some nations restrict foreign ownership
- Beware of minority protection

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## +/-: Costs & brand image control Licensing manufacturing rights

### Advantages

- Very low cost
- Royalty income

### Disadvantages

- Cost to monitor license compliance, especially QC
  - Risk to brand equity, TM
- Risk of lax IP enforcement in target country
- License registration?
- Foreign payment restrictions?
- Loss of distribution profit
- Reduced control, except by contract
- Tax Implications

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## +/-: Costs & brand image control Private Label

### Advantages

- Minimal costs
- Partner's distribution strength and scope

### Disadvantages

- No brand equity
- No control over marketing, sales or service
  - Can have performance standards
- Potential consumer protection liability

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## +/-: Control of resale prices

- **Reasons for control**
  - Brand image
  - Enhance profit margin for services
  - Cap profit margin for competitiveness
- **Regulation of RPM**
  - Varies by jurisdiction, even within US
  - Europe prohibits (pressure to comply with suggested resale price)
  - Latin America: Relative monopolistic practice
  - *Leegin*: US Supreme Court applies rule of reason
    - But anticompetitive in some circumstances
  - States may differ: NY, CA, NJ, MD, others
  - **Generally OK if unilateral – supplier makes “resale”**

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## +/-: Control of resale prices

### RPM Permitted

- Owned Outlets
- True Agents
- Controlled joint venture

### RPM Restricted

- Independent distributors
- Franchisees
- Licensees
- Minority joint venture

### Alternative methods

*Colgate* policy: Unilateral condition for dealing  
Minimum Advertised Price policy  
-- Condition for dealing  
-- Condition for co-op payments

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## +/-: Termination Rights

### Unrestricted

#### Subject to contract terms:

- Owned outlets
- True agency in US
  - Some payment requirements
- Most independent distributors
  - But Belgium
- Some franchises
- Most licenses

### Restricted

- Agents in EU (Mandatory compensation – Dir 86/653/EEC)
- In L.A by operation of law or old contracts prior to legal amendments
- Some U.S. franchises
  - Notably CA, NJ, WI, PR, VI
- Some industries, some states
  - Beer, wine, spirits
  - Auto dealers, gas stations
  - Farm equipment
  - Others

## +/-: Termination Rights

### • Typical restrictions:

- Good cause – narrowly defined
- Right to cure
- Right to renew
- Injunctive relief
  - May need to show irreparable harm
- Fair market value of distribution rights
- Unilateral modifications or certain discretionary prerogatives

## Lessons

- Differences are very fact-based and vary by jurisdiction
- The time to plan is *before* selecting a method of distribution

**Get knowledgeable local counsel  
early**

## Key Contract Provisions: Product Definition

- Specified products only
- All products under specified TMs
- All products meeting specifications
- Right of first refusal for new products
  - Same TM
  - Other TM
- Single agreement for all products
- “Most favored” provision

## Key Contract Provisions: Exclusivity

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- May supplier sell to others in territory
- May supplier sell directly in territory?
- Protection against gray market imports?
- Profit passover or invasion fees
- Reserved customers or categories
  - National or regional accounts
  - Invasion fees
- Internet sales

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## Key Contract Provisions: Exclusivity

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- **Distributors generally want exclusivity**
  - Avoids free-riding
  - Allows coordinated marketing of portfolio
  - Focus is on interbrand competition with competing brands, not intrabrand
- **Should suppliers want exclusivity?**
  - Do you want distributors competing with each other or with your competitors? On price or other metrics?
  - Does product require investment in:
    - Marketing and promotional events
    - Education and other pre-sales service
    - Warranty or other service

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## Key Contract Provisions: Restrictions on Competition

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- Competing products restrictions
  - Need to define specifically
    - **Beverages**
    - **Alcoholic beverages**
    - **Beer**
    - **Imported beer**
    - **German beer**
    - **Dark beers from Germany**
    - **Munich Oktoberfest style beers**
    - **Bottled Munich Oktoberfest style beers**
  - During term v. post-term

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## Key Contract Provisions: Restrictions on Competition

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- Ancillary to agreement's purpose
- Reasonable as to:
  - Duration
  - Geographic scope
  - Activities restricted

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## Key Contract Provisions: Indemnification and Insurance

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- Breaches
- Product liability, recalls
  - Distributor modification, storage, handling
- IP infringement
- Claims of prior distributor
- Proven claims v. alleged claims
- Liability insurance
  - Amounts
  - Additional named insured

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## Key Contract Provisions: Termination

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- Without cause where lawful
- Performance standards
  - Sales v. purchases
  - Sales v. execution
  - Consistency of enforcement
- Other breaches
- Changes in ownership or control
- Financial condition

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## Key Contract Provisions: Termination

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- **Notice**
  - Cure periods
- **Inventory repurchase**
  - Mandatory
  - One party's option
  - Mutual option
  - As agreed
- **Non compete/Non solicitation**

## Key Contract Provisions: Termination

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- **Compensation**
  - **Formula**
    - Sales multiple
    - Profit multiple
    - Others
  - Fair market value
  - Fair compensation encourages distributor investment
  - New distributor more likely to pay for rights

## Key Contract Provisions: FCPA Compliance

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- **Foreign Corrupt Practices Act prohibits bribery of foreign officials, political parties, candidates**
- **Strict liability for acts of controlled joint venture**
- **Liability for 3<sup>rd</sup> party acts – e.g., agents, distributors – if knowledge**
  - **Constructive knowledge, willful blindness, deliberate ignorance**

## Key Contract Provisions: FCPA Compliance

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- **Take steps before, in and after contract**
  - **Due diligence to vet potential partners**
  - **Contract provisions**
    - Representation that have not violated
    - Agreement to comply – spell it out
    - Reporting obligations, audit rights
    - Subdistributors require due diligence, approval
    - Provisions are material, ground for termination
  - **Ongoing training, monitoring, audits**



# Thank you

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## CONTACT:

- Andre R. Jaglom/L. Donald Prutzman
- Tannenbaum Helpen Syracuse & Hirschtritt LLP
- Tel: +1.212.508.6740/+1.212.508.6739
- Email: [jaglom@thsh.com](mailto:jaglom@thsh.com) / [prutzman@thsh.com](mailto:prutzman@thsh.com)
- Twitter: [@distributionlaw](https://twitter.com/distributionlaw)

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