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International Agency and Distribution Law

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In times of advancing globalization, companies are increasingly moving to new markets, especially in Asia, North America and the Middle East, in addition to the European domestic market. The distribution of goods and products in these areas, as well as the establishment of a necessary sales structure, is usually a worthwhile, yet not harmless challenge for entrepreneurs.

In addition to choosing the right distribution system, consideration must also be given to the respective country-specific characteristics, trade requirements and the legal framework during the drafting of distribution agreements. In contrast to the countries of the European Union (EU), which have harmonized the internal market with regard to the rights and obligations of commercial agents by means of Directive 86/653/EEC, there is a lack of such legal harmonization with reference to non-European countries.

Therefore, an entrepreneur is well advised on the one hand to carry out a legal review before setting up a new distribution branch abroad and on the other hand to have sales agreements drafted in accordance with the respective country-specific requirements. However, this is also necessary and advised in the case of doing business within the EU internal market, for example, when the distribution of products should take place through commercial dealers. This relates to the fact that a harmonized law for commercial dealers does not exist in the EU. In this regard, the respective country-specific regulations remain valid and applicable.

I. Distribution of products through commercial agents outside the European Union / European Economic Area

The following part discusses problematic issues that are typically relevant for entrepreneurs, which intend to distribute goods and products by means of commercial agents in countries outside the EU / EEA. It should be self-explanatory that within the framework of this summary, no in-depth country-specific or even general explanation of each individual aspect can be displayed. Rather, this summary aims to provide a first overview regarding the most relevant issues and create an awareness of possible risks.



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1. Definition

In German law, the term "commercial agent" is legally defined in Section 84 para 1 of the German Handelsgesetzbuch (hereinafter referred to as German Commercial Code/GCC). Pursuant this section, a commercial agent is defined as:

"a self-employed trader, who is constantly entrusted with the task of promoting or acquiring business for another entrepreneur."

This definition corresponds to the definition provided in article 1 para 2 of Directive 86/653/EEC. Only in cases where all criteria of section 84 para 1 GCC are fulfilled pursuant to the contractual design, the intermediary is to be regarded as a commercial agent.

If a company intends to distribute products to a country outside the EU by means of a commercial agent, the first legal difficulty in the foreign legal context can already be present in the desired legal classification of the intermediary as commercial agent. This is the case because the necessary delimitation to a commercial dealer, an employee or other forms of distribution is often achievable only by means of an explicit and precise regulation in the distribution agreement. For example, according to Turkish commercial law, the independence of the commercial agent is the decisive criterion for the delimitation to an employment contract. Therefore, an agency agreement which is governed by Turkish law must be highly aware of these requirements and must in no case contain regulations, which are likely to raise doubts as to the independence of the commercial agent.

In the event that the distribution agreement contains regulations contrary to the aforementioned requirements, this may eventually lead to a classification of the intermediary as an employee, for whom quite different legal regulations are applicable than for a commercial agent. This issue is even more acute when the foreign national law does not recognize a choice of law clause - for example, the choice of German law. However, it is also possible that foreign national law generally does not recognize different forms of distribution. Therefore, without exception, the foreign law might assume the validity of its commercial law with all of its consequences, including negative ones such as a goodwill indemnity or compensation claims. An example of such a regulation can be found in the agency law of the Dominican Republic.



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2. Status requirements

It should also be borne in mind that some countries already attach the status as commercial agent to certain conditions. For example, Qatar's agency law provides that only Qatar citizens or companies wholly owned by citizens of the emirate may be active as commercial agents. A commercial agent who has a different citizenship would therefore be unable to act in Qatar.

3. Exclusivity

A significant point of contract design is the question of exclusivity regarding the agency relationship. Existing exclusivity in favour of the agent has a significant influence on the principal's ability to act on his own in the contractual territory, either by himself or through third parties. Whether exclusivity can be agreed on individually or whether exclusivity is mandatory depends on the law of the destination country (i.e. the state in which the commercial agent is supposed to act), in case it applies to the commercial agency agreement because it is chosen by the parties or the respective regulation of the foreign law is a mandatory one.

Thus, in the United States of America, the contracting parties are basically free to agree on exclusivity, but exclusivity is not mandatory. Compared with this, the agency law of Brazil determines that, in the absence of a contractual regulation on exclusivity, such exclusivity is presumed. Pursuant Japanese law, a contractual exclusivity clause may constitute a violation of Japanese antitrust law, if the exclusivity prevents the commercial agent from entering into business with other principals. In case the law of the Kingdom of Jordan is applied, the latter would recognize a commercial agreement as an exclusive contract. This once again impressively demonstrates that a country-specific review is urgently recommended to any entrepreneur in the run-up to the negotiations and the design of agency and distribution agreements in general. Further on, such review enables the entrepreneur to ensure, if possible, an effective and clear contractual arrangement with regard to the issue of exclusivity.

4. Goodwill indemnity

A frequently asked question refers to the legal possibilities to exclude a possible compensation or goodwill indemnity claim of the commercial agent from the outset. However, it has to be stated that such exclusion is not possible within the EU and the EEA.



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Yet, regarding agency relationships situated outside the EU and outside the EEA, section 92c para 1 GCC stipulates that parties are free to deviate from the legal principle of goodwill indemnity. The exclusion of a goodwill indemnity or compensation claim is therefore possible in cases, where the distribution of goods of a (e.g.) German principal through a commercial agent situated in a state outside the EU/EEA is at hand and the applicability of German agency law is agreed upon.

However, the limits of the mandatory law of the destination country (i.e. the state in which the commercial agent is supposed to act) must be observed. Countries in the Middle East, in particular, regard the commercial agent's claim for indemnity as mandatory law and / or ordre public. Courts in these countries will therefore almost always deny the effectiveness of an exclusion clause. Moreover, they will not recognize or enforce foreign judgments and arbitration awards who deny indemnity claims for breach of the public order. For example, this is the case in the United Arab Emirates and Brazil. In such constellations, a basically possible exclusion of the goodwill indemnity claim of the commercial agent, which is in accordance with section 92c (1) GCC, is in vain. To know this in advance and to take appropriate precautions is essential for a company that intends to establish business via agents or distributors in these areas.

It should also be borne in mind that foreign laws sometimes determine the amount of the goodwill indemnity claim differently than domestic courts would do. For example, the terms "goodwill indemnity", "indemnity", "damages" or "compensation" are used abroad, which cannot necessarily be understood as a synonym for a (German) goodwill indemnity claim. This depends on the statutory regulations of the respective state. For example, the United Arab Emirates' law determines that compensation is usually a multiple of the annual average gain, which may be accompanied by a reimbursement of the "goodwill". Moreover, the courts of the United Arab Emirates are very protectionist and concerned with the protection of the local agents. In case of a dispute after the termination of the agency agreement, imports of the principal can be stopped or confiscated by national courts until the dispute between agent and principal is settled. Furthermore, the conditions under which a commercial agent can claim compensation against his principal differ from country to country.



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In contrast, a "good cause" existing in favour of the principal is often regarded as valid reason for the termination of the agency agreement and might lead to the elimination of a compensation claim. However, it is problematic to determine the existence of a "good cause". In most cases partial information is provided in the law of the respective country or by its courts. Conclusively, it is generally recommended to include "good causes" for terminating the agency agreement in a termination clause. If, subsequently, the principal terminates the agency agreement based on a good cause mentioned in the contract, this good cause could be used in a legal dispute to counter the compensation claim of the commercial agent as well. However, this possibility also depends on the concrete individual case and the specific country-regulations, if applicable.

5. Duration of the contract

In principle, there is the possibility to conclude an agency agreement for an indefinite or definite period of time. However, this presupposes that the applicable law permits a limitation at all. Thus, for example, the right of the People's Republic of China allows parties to freely determine the duration of the contract and the terms of the contract. To agree on a definite period of time may also have an effect on the possibilities for termination of the contract by the parties and compensation claims. In addition, statutory provisions must be observed, which may occasionally determine that, upon continuation of the expired temporary agency agreement, the latter will then be converted into an indefinite contract.

6. Formal requirements and registration requirements

It is also important to point out the formal requirements and / or registration requirements regarding the formation of an agency agreement, which exist in some states. For example, an agent who wants to work in Saudi Arabia needs a commercial agent license and must register himself with the commercial agent register at the Saudi Ministry of Economic Affairs. The registration has only a declaratory effect, but non-registration can be sanctioned with penalties. Further formal requirements exist with regard to the prerequisite for registration of the agency agreement.

However, registration can prove to be dangerous for the principal in the long term, since only one commercial agent can be registered with the Saudi Ministry of Economic Affairs. If a dispute arises between a principal and an agent regarding the validity of the termination, the agent can block the registration of a new agent. In many cases, the principal won't have



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another choice than to pay the terminated agent a high amount of money in order to receive his consent to register a new agent.

7. Choice of law

Each contracting party prefers the familiar (domestic) law in the context of contractual arrangements. However, even if a choice of law is generally recognized in the destination country, such choice can lead to problems regarding an exclusion of the compensation claim. This is because a domestic court most likely won't recognize the choice of law, if the respective agency agreement excludes a goodwill indemnity claim, even if such exclusion is admissible under the chosen law (e.g. for reasons of public order or mandatory law). In case there is an additional jurisdiction or arbitration clause within the agency agreement, there is a risk that the domestic court will neither recognize nor enforce a decision of a foreign court or an international arbitral tribunal. Thus, an initially possible exclusion of the compensation claim may be ineffective in the end.

Lastly, the United Nations Convention on Contracts for the International Sale of Goods (CISG) must always be kept in mind. If its application is not expressly excluded in the agency agreement, the parties risk that it may inadvertently be applied.

8. Jurisdiction and arbitration clauses

As stated with regard to a choice of law, an effective jurisdiction or arbitration agreement initially presupposes that the law of the foreign state recognizes such agreement and enables enforcement of the judgment / arbitration award.

In the case of arbitration agreements, enforcement in the destination country is at first glance easier, since the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards has been ratified and implemented almost worldwide and allows for rapid enforcement. However, it is also necessary to examine, whether there are any obstacles to enforcement. Such may be given, in particular, in the event of infringement of mandatory law or norms of public policy.



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II. Distribution of products through commercial dealers

The following is a list of those issues that typically arise when commercial dealers, on behalf of a supplier or manufacturer, sell goods.

1. Definition

In Germany, there are no laws regarding commercial dealers, so that no legal definition of the dealer can be found. Jurisprudence therefore had to create a definition of the dealer. A commercial dealer is someone

"who as an independent trader is constantly entrusted with the task of carrying out business for another entrepreneur in his own name and for his own account."

The commercial dealer's definition is therefore similar to the definition of the commercial agent in section 84 para 1 GCC. The contractual agreement is also concluded for a certain period of time. The dealer agreement is a framework contract, by which the dealer is more or less incorporated in the sales organization of a manufacturer or supplier. Contrary to the commercial agent, however, the commercial dealer does not negotiate or arrange business, but buys goods in his own name and for his own account, in order to sell them in his own name and for his own account. The individual purchase contracts by which the dealer purchases goods from the manufacturer or supplier are therefore to be distinguished from the framework contract.

In other countries, it is necessary to examine whether the respective national law provides legal provisions applicable to the dealer, subordinates him to the regulations of the commercial agent, or leaves the parties complete contractual freedom. In Germany, for example, certain rules - and especially the right to goodwill indemnity - may be applied by way of analogy to the commercial dealer under certain conditions.

2. Compensation claim, exclusivity, choice of law, etc.

The same questions with regard to a possible goodwill indemnity claim, exclusivity, formal requirements, duration of contract, choice of law, jurisdiction and arbitration agreements arise, which were discussed above referring to the commercial agent. As a matter of principle, the previous comments on the commercial agent apply in many respects to the



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trader as well. However, due to the many different distribution laws in the various countries, it is difficult to present a summary here.

III. Outlook

The international distribution of goods and products by means of commercial agents and commercial dealers holds many economic opportunities, but also some risks for the ambitious entrepreneur. At the same time, many of these risks can be identified and avoided in advance, so that the establishment of a new distribution system - after a well-founded and comprehensive legal advice - is possible.

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