

Suppliers often depend on distributors to open up markets more efficiently, more quickly and less expensively than they can themselves. These relationships can often be very successful, but suppliers and distributors should be careful to avoid some common problems.

Make Your Agreement Flexible and Mutually Beneficial

Sometimes suppliers with a new product engage distributors on terms which they later regret. The pricing, payment terms, exclusive rights, or territory may be too generous. They may be better to start a new distributor with a small territory and expand it gradually if business goes well. A supplier may also be better to tie exclusive rights to sell in a certain market to achieving specific sales targets. Likewise, distributors eager to sell new products may accept terms which are too burdensome or expensive.

A distribution agreement should be designed to serve both parties over the long term. A one sided contract may be tolerated when business is good, but when difficulties arise the agreement will probably be breached or terminated - and dealing with such an outcome can be expensive.

Protect Your Intellectual Property

Before appointing a distributor, suppliers should protect their intellectual property by registering trademarks or patents in the appropriate jurisdiction. There should also be a clear agreement on the distributor's use of the supplier's trade-marks and what happens when the relationship ends.

Distributors should be careful about investing a lot of money in marketing a trade-mark they do not own. Ideally, marketing costs should be shared.

Clarify Matters Concerning Termination

A simple written agreement can clarify several issues for the parties, including how the agreement can be terminated and what notice is required. Unless a contract states otherwise, if there has been no default and one party terminates, that party has an obligation to give reasonable notice to the other party. Generally more notice is required if there has been a long and close relationship between the parties.

Suppliers usually prefer an agreement limited to a certain period of time rather than an "evergreen" agreement which automatically renews itself until terminated. One problem with an evergreen agreement is that it can postpone resolution of ongoing issues and tensions.

Know the Other Party

Before entering a distribution agreement, a business should make sure it has realistic expectations of what it can accomplish. It can be tempting - but also dangerous - to promise more than what can be delivered.

For this reason it is important for each party to learn as much as possible about the other. It is better to rely more on facts than on impressions or reputation, and on explicit written terms than on assumptions.

It is also important to monitor changes in management and owners, news about the business and its performance, and trends in the promptness of payment. If a business knows the other party well and can anticipate changes, it will be in a better position to deal with problems and maintain a positive relationship.

Avoid Depending on One Supplier or Distributor

Often a distributor depends on one or two key suppliers. Suppliers may also be dependent on only a few distributors. This is more a business issue than a legal one, but it will affect the position of the parties in negotiating a distribution agreement.

Unintended Legal Consequences

Suppliers and distributors should be careful not to inadvertently trigger legal issues. For example, Ontario has a franchise law which imposes onerous disclosure obligations on franchisors. Suppliers/distributors should be careful not to create a contract with their customers which unknowingly creates a franchisor/franchisee relationship.

In addition, the *Competition Act* of Canada has serious penalties, both civil and criminal, for suppliers/distributors who contravene the restrictive trade practices provisions of the law. Contracts with customers should be written with this in mind.

Suppliers and distributors should share a clear understanding of their legal obligations. With that foundation, they can build a successful and durable relationship.

These issues can be complicated; if you have any concerns or would like more information on this topic, please contact Houser Henry & Syron at info@houserhenry.com and one of our lawyers will be in contact with you.

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