

Distribution & Agency

Contributing editor
Andre R Jaglom



2019

GETTING THE
DEAL THROUGH

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Tannenbaum Helpern Syracuse & Hirschtritt LLP

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Preface

Distribution & Agency 2019

Fifth edition

Getting the Deal Through is delighted to publish the fifth edition of *Distribution & Agency*, which is available in print, as an e-book and online at www.gettingthedealthrough.com.

Getting the Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique **Getting the Deal Through** format, the same key questions are answered by leading practitioners in each of the jurisdictions featured.

Getting the Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.gettingthedealthrough.com.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Getting the Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editor, Andre R Jaglom of Tannenbaum Helpert Syracuse & Hirschtritt LLP, for his continued assistance with this volume.

GETTING THE
DEAL THROUGH 

London
February 2019

Global Overview

Andre R Jaglom

Tannenbaum Helpern Syracuse & Hirschrift LLP

Global commerce depends, to a very great extent, on the relationships between manufacturers and suppliers, on the one hand, and their distributors and commercial agents around the world, on the other. These relationships are the linchpin to moving goods and services to new markets around the world, and they are governed not only by the contracts negotiated between suppliers and their distribution partners, but by a wide range of laws and regulations, which vary widely from country to country. Developments in areas such as privacy and data protection and increasing concerns over cybersecurity affect distribution relationships as well, as a result of the normal sharing of customer information and other data between distribution partners.

With the growing importance of e-commerce, consolidation by mergers and acquisitions at all levels of distribution chains that create larger suppliers and distributors in industry after industry, and new forms of relationships between suppliers and distributors that are created to meet developing needs of businesses, the global distribution and marketing of products in today's economy raise a host of legal questions with different answers in each jurisdiction. The effective distribution lawyer must understand the client's business objectives, culture and industry, and then apply the legal and regulatory environment of each jurisdiction to help the client find the most effective, least risky method, among many alternatives, of bringing its goods or services to market.

Those alternatives cover a spectrum of possibilities, from direct distribution by the supplier itself or through a wholly owned subsidiary; to engagement of a local commercial agent that does not take title to the goods, arranges sales on behalf of the supplier and receives a commission; to independent distributors, which buy from the supplier and resell in the market country at a profit; to franchising, which amounts to the use of independent distributors that are licensed to use the supplier's trademarks, required to follow a prescribed marketing plan or method of operation, and pay a franchise fee to the supplier. All these options may be implemented through a joint venture by having the local distribution entity owned in part by the supplier, or the revenues and expenses shared in another manner. Another option is for the supplier to license a manufacturer in the market country to use its intellectual property – patent, copyright, trademark or trade secrets – to make its products locally and sell them. And private label methods amount to a reverse licensing arrangement, where a distributor or retailer in the market country distributes the supplier's products under its own trademark.

These options carry different costs, levels of control and sharing of revenues, different legal and business risks, tax consequences and potential liability. Guiding clients through these options requires counsel to understand the clients' objectives, culture and ways of doing business, industry customs and practices, as well as the legal environment in the relevant jurisdictions. And the growing role of e-commerce, the borderless nature of which inherently disrespects distribution territories, complicates the achievement of the objectives of distribution partners. It makes the protection of distributor territories more difficult, and thereby weakens distributor incentives to provide promotional, educational, warranty, quality control and merchandising services for products whose sales revenue may go elsewhere. Counsel must help their clients find ways to compensate for lost sales and restore appropriate incentives without running afoul of competition laws and other regulatory obstacles.

The practice of distribution law is necessarily interdisciplinary, for assisting clients in structuring and managing distribution relationships requires an understanding of each relevant jurisdiction's contract law; antitrust and competition law; dealer protection and business franchise law; privacy and data protection laws; consumer protection laws; advertising and unfair competition regulation; intellectual property law; international trade law; mergers and acquisitions law; and litigation, arbitration and dispute resolution.

By way of example, Europe provides for an indemnity payment on termination of commercial agents without good cause, but not for distributors – except in Belgium, where distributors are covered. The United States has no such provision – except for a few states' business franchise laws and laws governing certain industries – yet Puerto Rico, a US territory, has one of the most stringent laws in the world protecting distributors.

The collection and transfer of consumer data is tightly regulated in Europe, Canada and many other countries. Except for certain industries and types of data (eg, financial firms, children's data and medical information), the US, at least on a national level, adopts a much more laissez-faire approach, requiring principally that US businesses give clear notice of their data collection and transfer practices and then abide by their promises, and secure personal information appropriately, with little substantive regulation. This difference in attitude came to a head in October 2015 in the *Schrems* case, when the European Court of Justice, based on its understanding of US government access to personal data (an understanding deemed erroneous by the US), invalidated the Safe Harbour arrangement by which US companies that subscribed to its principles could receive personal data from European affiliates and trading partners. The 2016 replacement 'Privacy Shield' arrangement remains subject to challenge. So long as US authorities claim the right to intercept, collect and review communications without a showing of particularised need, the problems identified in the *Schrems* case may potentially be found to apply to the Privacy Shield as well, complicating the sharing of information between the EU and the US.

Moreover, increased cybersecurity concerns have led to regulations at both the federal and state levels imposing security standards and breach notification requirements on businesses. The European General Data Protection Regulation also imposes far-reaching obligations to honour individual privacy and data protection rights. Where applicable, businesses must ensure that those with whom they share protected data comply with these requirements as well. This means that distribution and agency agreements need to address these issues.

Supplier control of resale prices is generally illegal in Europe, as are prohibitions on sales by distributors over the internet or outside of defined territories, but in the United States all are typically permitted, with some exceptions.

In most jurisdictions the licensing of intellectual property such as trademarks between suppliers and their distribution partners is a matter of private contract. However, some jurisdictions, such as Mexico, require trademark licences to be publicly filed.

Even within a jurisdiction, different industries have different customs and practices that have a practical effect on how distribution relationships are structured. In the United States, for example, beer distributors share detailed data on their sales to customers with their suppliers on a monthly – and for the larger brewers, daily – basis, but

soft drink bottlers and distributors zealously guard such customer sales data and generally will not share them with suppliers.

These legal and practical differences can have a major impact on how suppliers and their distribution partners do business, and counsel cannot possibly give sound advice without an understanding of these major differences in the regulatory framework and industry practices around the world.

While *Getting the Deal Through – Distribution & Agency* will not make you an expert in all the relevant laws of every jurisdiction, it will provide a handy reference for the key issues in many important jurisdictions. It will remain essential to engage qualified local counsel with expertise in the many facets of law affecting distribution before embarking on distribution in a new market, but this book should enable you better to understand the issues and the questions to ask.

Belgium

Olivier Vanden Berghe and Sebastian Tytgat
Liedekerke Wolters Waelbroeck Kirkpatrick

Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

A foreign supplier is entitled to establish its own entity to import and distribute its products in Belgium, as the freedom to perform economic activities is one of the basic freedoms established in Belgian law.

Belgian authorities can in principle impose restrictions, but European legislation (specifically the freedom of establishment as laid down in articles 49 to 55 of the Treaty on the Functioning of the European Union) always has to be respected.

For some specific sectors (eg, credit agents, insurance agents), prior approval or permission by the authorities is required.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Insofar as such ownership would not infringe Belgian and or European competition law (which would depend on the specific circumstances of the case), a foreign supplier may indeed incorporate a local Belgian company together with its supplier.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

The most important distinction to be made is the one between business entities without limited liability and those with limited liability. As the importer would engage in economic activities, which would inherently involve a certain amount of risk, a limited liability entity is preferable. Such a limited liability entity would limit its shareholders' liability to the equity investment in case of bankruptcy.

The most common types of limited liability business entities in Belgium currently are:

- private limited liability company (BVBA/SPRL); and
- public limited liability company (NV/SA).

The BVBA/SPRL and the NV/SA are governed by the Belgian Company Code. Both types of entities must be incorporated by way of a notarial deed and require the filing of an extract of such deed, consisting of, among others, the articles of association and details of the incorporators, with the clerk's office of the competent commercial court (to be determined based on the location of the registered seat).

It should, however, be noted that important changes to Belgian company law are expected to enter into force in 2019.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

Safe from specific requirements for certain regulated sectors (eg, banking), Belgian law does not include a general principle restricting the economic freedom of foreign businesses. Within the framework of the European Union, the free movement of persons, services and capital, and the freedom of establishment are basic principles.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

A foreign supplier is entitled to own an equity interest in the local Belgian entity distributing its products.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

Non-residents, whether natural persons or corporations, are taxed only on Belgian source income; that is, income produced or collected. Certain types of income are subject to withholding tax that may either be credited against the global tax liability or constitute the final tax liability.

A foreign corporation is subject to non-resident income tax in Belgium if it has an 'establishment' in Belgium. However, even without an establishment, a foreign company may be taxed on its Belgian-source income. Branches of foreign companies are taxed at the same rate as resident companies (29.58 per cent for income sourced in 2018 and 2019, and 25 per cent for income sourced as from 2020 – subject to changes made by future government decisions). The taxable profit is determined as for Belgian corporations.

However, national rules of Belgian tax legislation might be subject to prevailing international law (eg, double taxation treaties). Typically, under such treaties (if any), Belgian branch income is exempt in the resident state and Belgian withholding tax levied on dividends, interests and royalties is limited.

Aside from income tax, the provision of goods and services in Belgium is in principle subject to VAT (general tariff of 21 per cent, by exception 6 per cent or 12 per cent). Moreover, European legislation provides for customs duties levied on the importation of products from outside the European Union. Finally, there is a wide variety of taxes imposed by local governments (provinces, municipalities, etc) or applicable to specific sectors (eg, banking and insurance, fuel, tobacco and alcohol, etc).

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

The most common distribution structures under Belgian law are the following:

- commercial agency: the supplier can charge a commercial agent with the negotiation and possibly even the conclusion of business deals on behalf of and in the name of the supplier. Commercial agency is regulated by articles X.1 to X.25 of the Belgian Code of Economic Law, which provide for a quite strict regime;
- distributorship: the supplier can grant a distributor the right to sell, in the distributor's own name and for its own account, goods manufactured or sold by the supplier. The Belgian legislator has provided for quite strict legislation regarding the termination without cause of exclusive distribution agreements of indefinite term (articles X.35 to X.40 of the Belgian Code of Economic Law). The supplier can also opt for a non-exclusive distribution or a selective distribution network in the EEA;

- franchising: a franchisor is an independent intermediary offering goods or services in its own name and for its own account according to a (long-term) right (and obligation) to use the commercial concept of the franchisor or supplier; and
- commission brokerage is a less frequented distribution structure, whereby the supplier appoints a 'commission broker' to act in its own name but on behalf of the supplier. Most frequently, the commission broker's activity as an intermediary is of a logistic and operational nature.

The Belgian legislator has provided for specific rules regarding pre-contractual information within the framework of commercial cooperation agreements (articles X.26 to X.34 of the Belgian Code of Economic Law), that apply to franchising and possibly to commercial agency, distributorship and, although quite unlikely, to commission brokerage. It is crucial to seek legal counsel before establishing a distribution network in Belgium.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

Regarding the precise legal qualification of the relationship between a supplier and its distributor, the legislation mentioned in question 7 will be applicable.

Both Belgian and European competition law also have to be abided by and are enforced by the Belgian Competition Authority and the European Commission (mainly prohibition of restrictive practices and the abuse of a dominant market position).

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

If the distribution relationship is not regulated by mandatory commercial agency legislation (articles X.1 to X.25 of the Belgian Code of Economic Law, see question 7) or by mandatory distribution legislation (articles X.35 to X.40 of the Belgian Code of Economic Law, see question 7) the possibility of termination depends on the term of the relationship:

- contractual relationships of indefinite term can always be terminated by giving a 'reasonable' termination notice or indemnity in lieu of notice, which would depend on the practical circumstances of the relationship. In practice, the contract will often provide for a well-defined notice period or termination formalities;
- contractual relationships of definite term can in principle not be terminated before the expiry of said term, unless the parties have provided for a contractual early termination clause. A decision not to renew a contractual relationship would, under general Belgian contract law, not be a termination decision; and
- both contractual relationships of determined and indefinite term can be terminated for cause by any party in case of gross negligence. In theory, the termination should be claimed before a court but, in practice, the parties generally contractually provide for a possibility to terminate for cause without prior intervention from a court.

Belgian legislation on termination without cause of exclusive distribution agreements of indefinite term provides that contracts falling within its scope cannot be terminated without cause otherwise than with a 'reasonable notice period' or a 'fair indemnity' in lieu of notice. The length of the notice period or the amount of the indemnity in lieu of notice can be agreed upon between the parties only after termination of the agreement. If the parties fail to reach an agreement, the courts decide according to the principles of 'equity'. One must, however, be cautious as said mandatory legislation provides for specific conditions under which agreement of definite term will be assimilated to agreement of indefinite term.

Belgian mandatory commercial agency legislation provides for a minimum notice period of one month per started year, with a

maximum of six months. This mandatory period of notice is applicable to commercial agency agreements of indefinite term. It does not apply to agreements of definite term, except when a clause allows termination without cause prior to the expiry date. The party terminating the commercial agency agreement without granting the minimum period of notice must pay a legally defined termination indemnity.

Any commercial agency agreement can be terminated for cause when exceptional circumstances render any further cooperation between the parties definitively impossible or in case of a material breach by the other contracting party. The terminating party would have to abide by very short and strictly defined delays, as well as formal requirements.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

In case of valid termination for cause, no mandatory compensation or indemnity would be due by the terminating party. However, in practice, a termination for cause will often be disputed and lead to discussion between the parties.

The party terminating without cause a commercial agency agreement falling within the scope of mandatory legislation (see questions 7 and 9) without granting the minimum period of notice must pay a termination indemnity, which will be equal to the agent's remuneration, calculated on the basis of the average amount of commissions earned during the 12 months prior to termination, which would have been due if the notice period had been granted. Moreover, a goodwill indemnity might be due if certain conditions are met. The amount of the goodwill indemnity is limited to a maximum of one year of commission calculated on the basis of the average amount of commission earned during the five years prior to the termination.

The party terminating without cause an exclusive distribution agreement falling within the scope of mandatory legislation (see questions 7 and 9) without granting a 'reasonable notice period' must pay an indemnity in lieu of notice, which is usually computed on the basis of the 'average semi-gross profits' made by the distributor during the last two or three years of the relationship. Moreover, an 'equitable complementary indemnity' might be due if certain conditions are met. The amount of the indemnity is fixed rather arbitrarily in Belgian case law.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

A clause prohibiting the transfer of the distribution rights, the ownership or business to a third party are in principle valid and enforceable under Belgian law. As distribution relationships are often *intuitu personae* (meaning that the counterparty's identity is crucial to the agreement), such clauses are common.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

In practice, it is recommended to draft confidentiality clauses as wide as possible, as business secrets are not protected 'as such'. If the information concerned has been made public prior to entering the agreement or if the information concerned is considered to be of 'general knowledge', it cannot be considered as confidential.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

A commercial agency agreement can contain a non-compete clause, which will only be valid, however, if and to the extent that:

- it is made in writing;
- it relates to the specific types of transactions assigned to the agent;
- it is limited to the geographical area or to the group of customers and the geographical area entrusted to the agent; and
- its application is limited to a term not exceeding six months after termination or expiry of the agreement. Furthermore, the representation of competing products by the agent could also be

perceived as a violation of his or her obligation to act in the best interests of the principal and to be loyal and of good faith.

Distribution agreements very often comprise restrictions on the distribution of competing products, which are admitted to a certain extent. In this regard, it is important to highlight that the Commission Regulation (EU) No. 330/2010 excludes certain non-compete arrangements from the 'block exemption' (eg, any direct or indirect obligation causing the buyer, after termination of the agreement, not to manufacture, purchase, sell or resell goods or services). Under said regulation, a supplier can impose a non-compete obligation on its distributor, insofar as it is imposed for a fixed term of no more than five years.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

Suppliers may not restrict the buyer's ability to determine its sale price, without prejudice to the possibility of a supplier to impose a maximum sale price or recommend a sale price, provided that they do not amount to a fixed or minimum sale price as a result of pressure from, or incentives offered by, any of the parties.

These restrictions are enforced by the competition authorities, national or European, which can impose substantial fines to perpetrators.

The supplier may determine the price offered by a commercial agent to the customers, since the commercial agent acts in the name and for the account of the supplier.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

As a general rule, the supplier may not, directly or indirectly, in isolation or in combination with other factors under its control, restrict the distributor's ability to determine its sale price. However, it is possible for the supplier to impose a maximum sale price or suggest a sale price, provided that they do not amount to a fixed or minimum sale price as a result of pressure from, or incentives offered by, any of the parties. Where a minimum advertised price policy would be valid in principle, the refusal to deal with customers who do not follow its pricing policy would in principle not be valid.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

A distribution agreement may in principle include a clause stipulating that the supplier's price to the distributor will be no higher than its lowest price to other customers (a 'most favoured customer' clause).

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

Considering that contractual freedom is a cornerstone of the Belgian legal order, the seller can in principle differentiate its prices, insofar as such differences are not in violation of competition law, consumer legislation and possible regulatory provisions that might be applicable, and it does not constitute an abuse of rights.

To avoid being dragged into a discussion or even litigation based on an alleged violation of the anti-discrimination regulation, it is recommended to underpin differentiated prices with objective reasons (eg, transport costs, marketing, volumes, etc).

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

The answer to this question depends on the type of distribution used by the supplier.

It is possible to impose restrictions on the activities of the exclusive distributors outside their territory: active sales outside the territory may be prohibited insofar as the conditions of EU Regulation No. 330/2010 are abided by, whereas passive sales outside the territory must at all times be allowed. The supplier can prevent its exclusive wholesale distributors from selling to end users and consumers (both active and passive selling). However, if a supplier allocates a particular customer group exclusively to a specific distributor active at the retail level, the supplier cannot impose a restriction on passive sales towards such a customer group by the other distributors.

Non-exclusive distributors can, in principle, not be prevented from engaging in passive sales, but they may be subjected to territorial restrictions concerning their active sales outside their territory, insofar as the conditions of EU Regulation No. 330/2010 are abided by. The same rules applicable to customer allocation (wholesale and retail) with exclusive distribution apply to non-exclusive distribution.

If a supplier operates an EEA-wide selective distribution network, the supplier may not impose territorial restrictions, apart from a location clause. The active and passive sales to consumers by members of such a network may not be restricted. The same rules applicable to customer allocation (wholesale and retail) with exclusive distribution apply to selective distribution.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

The answer depends on the type of distribution used by the supplier.

In exclusive distribution, it is not possible to prevent the exclusive distributor from having passive sales (eg, e-commerce sales) outside its contract territory. However, the supplier can restrict the exclusive wholesale distributor to refrain from selling to end users and consumers. This is also true for e-commerce (passive sales). However, if a supplier exclusively allocates a specific customer group to a retail distributor, passive sales by other distributors cannot be restricted by the supplier.

E-commerce sales by non-exclusive distributors can not in principle be restricted by the supplier. However, the same rules applicable to customer allocation (wholesale and retail) with exclusive distribution apply to non-exclusive distribution.

The supplier must restrict the ability of a distribution partner that is part of a selective distribution network to engage in active or passive sales to resellers that are not part of said network. A supplier may prohibit its distribution partners that are part of a selective distribution network from using, in a discernible manner, third-party platforms for internet sales of the goods in question, provided that:

- such prohibition has the objective of preserving the luxury image of the goods in question;
- it is laid down uniformly and not applied in discriminatory fashion; and
- it is proportionate in the light of the objective pursued (European Court of Justice case of 6 December 2017, C-230/16).

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

A supplier wishing to refuse to deal with particular customers must make sure that such refusal cannot be considered as a restrictive practice, an abuse of a dominant market position or an abuse of the right to contractual freedom (see question 17). To avoid being dragged into a discussion or even litigation, it is recommended to underpin a refusal with objective reasons.

A supplier may restrict:

- the active sales to an exclusive customer group reserved to the supplier or allocated by the supplier to another distributor where such a restriction does not limit sales by the customers of the distributor;
- the sales to end users by a distributor operating at the wholesale level of trade;
- the sales by the members of a selective distribution system to unauthorised distributors; and
- the distributor's ability to sell components supplied for the purposes of incorporation, to customers who would use them to manufacture the same types of goods as those produced by the supplier (see question 18).

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

Any merger of a certain scope requires prior approval of the national competition authority or the European Commission.

A distribution or agency agreement might only be reportable if it qualifies as a 'merger' operation under Belgian law; that is, a lasting change of control of an undertaking, which can particularly occur when two independent undertakings decide to integrate; when one undertaking or one person having control of an undertaking purchases another undertaking or part of its activities; or when two undertakings create a lasting common undertaking between them (article IV.6 of the Belgian Code of Economic Law).

Notification to the competition authorities would only be required for mergers that meet certain turnover thresholds. For the relatively small mergers, the Belgian Competition Authority will deal with the case (articles IV.7 to IV.10 of the Belgian Code of Economic Law). For larger mergers (generally having effects that extend beyond national borders), the notification will have to be made to the European Commission (Council Regulation (EC) No. 139/2004 of 20 January 2004 on the control of concentration between undertakings).

In practice, the parties to sizeable transactions will often stipulate that the operation is subject to such prior approval.

In short, the procedure comprises a notification to be made to the competent competition authority (usually following informal pre-notification communication with said authority). It is then up to the authority to define the market concerned and to examine the merger's likely effects on that market. A first decision will be made, which can be followed by a second phase procedure where there are serious doubts as to the merger's eligibility.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

In general, anticompetitive behaviour is sanctioned both by national and EU legislation. Regarding the impact of such behaviour on intra-community trade, the matter will be dealt with by the national or the European competition authorities (see question 21), which can impose fines.

On 26 November 2014, the European Parliament and the European Council adopted Directive 2014/104/EU on certain rules governing actions for damages under national law for infringements of the competition law provisions of the member states and of the European Union. This Directive has been transmitted in national law through the Act of 6 June 2017 allowing any natural or legal person who has suffered harm caused by an infringement of competition law to claim and to obtain full compensation for that harm through damages actions before national courts.

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

First, if a distributor sells the supplier's products in the exclusive territory or to the exclusive group of customers awarded to another distributor, the latter would in practice address the supplier that has granted the exclusivity rights to notice the infringing distributor to refrain from encroaching on said exclusivity. If the supplier refuses to assist the exclusive distributor in defending its exclusivity rights, this will often lead to discussion and even litigation.

Second, an authorised distributor that is part of a selective distribution system will also address the issue of unauthorised sales to the supplier, which is responsible for safeguarding the network's identity. Most often, the issue will involve an authorised distributor that does not respect the prohibition of sales outside the selective distribution network. Both the supplier and other prejudiced authorised distributors can claim compensation from the infringing distributor.

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

The answer depends on the type of distribution used by the supplier.

The supplier can, in principle and within certain legal boundaries, restrict the exclusive distributor's activities outside its territory. For example, active sales outside the territory may be restricted if it concerns sales to territories that the supplier has reserved for itself or which it has allocated to an exclusive distributor, if the conditions provided by EU Regulation No. 330/2010 are abided by. Moreover, the supplier may prevent its exclusive distributor from changing its primary place of establishment, or from opening additional outlets, showrooms and warehouses and the supplier may restrict the exclusive wholesale distributor's ability to actively and passively sell to end users or consumers (see question 19).

Non-exclusive distributors may be subjected to territorial or customer restrictions insofar as the conditions of EU Regulation No. 330/2010 are abided by.

If the supplier operates a selective distribution network in the EEA, no territorial restrictions may be imposed by the supplier, other than a location clause. A selective distributor may not be prevented from active or passive sales towards end users in the EEA, unless the selective distributor solely operates on the wholesale level.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

One must distinguish industrial property rights from literary or artistic property rights.

Industrial property rights concern creations that play an economic role in production and distribution processes, and may be protected by patents, plant variety rights or design rights. Moreover, industrial property rights can also apply to distinctive signs such as trademarks or geographical indications. Even though trade names and legal names are not intellectual property rights as such, they also benefit from certain kinds of protection. Most industrial property rights are obtained through a formal procedure, most often comprising registration requirements.

Literary and artistic property comprises copyrights and related rights (eg, photographs, music, literary works, etc). Furthermore, literary and artistic property rights also protect rather technical creations, such as software, databases and topographies and electronic chips. Copyrights and related rights automatically come into effect at the time of creation.

It must be noted that know-how as such is not covered by specific legal protections and, as simple ideas, may generally be protected by confidentiality clauses or non-disclosure agreements (see question 12).

Infringement of one's intellectual property rights can be countered through various ways: a complaint can be filed with the Federal Department of Economy or summary proceedings can be initiated to stop such infringement, among others.

In Belgian distribution and agency practice, technology-transfer agreements and, more specifically, the licensing of know-how, is common. Such agreements are regulated by, among others, the Commission Regulation (EU) No. 316/2014 of 21 March 2014 on the application of article 101(3) TFEU to categories of technology-transfer agreements.

26 What consumer protection laws are relevant to a supplier or distributor?

The most notable pieces of legislation that have to be taken into account by the supplier or distributor are Book VI of the Belgian Code of Economic Law on Trade Practices and Consumer Protection and sections 1649-bis to 1649-octies of the Belgian Civil Code on Consumer Sales.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

Both suppliers and distributors have the obligation to provide safe products and have to immediately warn both customers and the

government (the Belgian Federal Department of Economy) of any issues that might arise. The law obliges the supplier to take corrective measures including a recall if needed.

The contract may delineate which party is responsible for absorbing the cost of a recall. The carrying out of the recall will be up to the supplier, but the distributor is legally obliged to cooperate. In practice, the absorption of the cost of the recall will often lead to a discussion and even litigation.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

As the relationship between the supplier and its distribution partner is a business-to-business relationship, the supplier can use its contractual freedom to limit its warranties provided to such partner. However, that limitation has boundaries. An exemption clause taking away the essence of the obligations of a contracting party or restricting liability in case of wilful misconduct will be considered unlawful.

Second, business-to-consumer relationships are subject to regulation with a view to protecting the consumer, meaning that the supplier cannot validly limit or exclude its warranties towards end customers.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

Specific legislation applies to the processing of personal data (eg, on 25 May 2018, the European General Data Protection Regulation (GDPR) came into effect).

Specific regulations apply to the transfer of personal data to countries outside the EER that do not offer an adequate level of protection (eg, the United States). Expert advice is strongly recommended.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

As a distribution relationship is construed between two independent parties, the supplier may, in principle, not approve or reject the distribution partner's managing personnel, or terminate the relationship out of mere disagreement with the distributor's management's decision, insofar as the decision does not constitute a breach of contract.

However, contractual freedom allows the parties to provide for key-person clauses. These clauses are often used in practice and allow for the termination of the contract by a party in case of a change in the management or ownership of the other party.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

A distributor or agent could indeed be considered an employee of the supplier if the factual circumstances show that the latter exercises authority over the distributor or agent, who would be in a subordinate position (eg, no freedom to organise work and time).

If a distributor or agent would be qualified as an employee, there would be serious consequences for the supplier, such as retroactive recovery of social security contributions and taxes due, administrative fines and even criminal sanctions.

The supplier must make sure that the distributor or agent has the freedom to organise its professional activities as it sees fit, and that they can operate as truly independent business entities.

32 Is the payment of commission to a commercial agent regulated?

The principal and agent are free to agree on the agent's remuneration, which may consist of either a fixed amount or commissions or a combination of both.

If the remuneration consists at least in part of commissions, the agent shall be entitled to a commission on business deals concluded during the period covered by the commercial agency agreement where:

- the business deal is concluded as a result of the agent's activities;
- the business deal is concluded with a third party whom the agent had previously acquired as a customer for business deals of the same nature; or
- the agent has an exclusive right to a specific geographical area or group of customers and a business deal has been entered into with a customer belonging to that area or group.

The agent is also entitled to commission for business deals concluded after the termination or expiry of the commercial agency agreement where:

- the business deal is mainly attributable to the agent's efforts during the period covered by the commercial agency agreement and the business deal is entered into within a period of six months of the termination or expiry of the commercial agency agreement; or
- the order of the customer reached the principal or the agent before the commercial agency agreement expired or was terminated.

The parties are free to agree on the exact moment the commission becomes due and payable. However, notwithstanding any provision to the contrary, the commission becomes due at the latest when the customer has performed his or her part of the business deal or when he or she would have done so if the principal had duly performed his or her part of the business deal, and the commission must be paid not later than on the last day of the month following the quarter in which it became due.

The parties may agree (in writing) that the right to commission will extinguish but only if and to the extent that:

- the customer does not perform his or her part of the transaction, except when the non-performance is due to circumstances imputable to the principal;
- the performance of the business deal has become impossible, unless this would be imputable to the principal; and
- the performance of the business deal cannot reasonably be imposed on the principal, especially when there are serious reasons that justify the non-performance by the principal and that are imputable to the customer.

33 What good faith and fair dealing requirements apply to distribution relationships?

There are no specific provisions on good faith and fair dealing requirements for distributors under Belgian law. However, the general obligation to perform contractual agreements in good faith applies (section 1134 of the Belgian Civil Code).

The commercial agent is expressly obliged to act in the best interest of the principal, to be loyal and of good faith. This means that the agent shall act in accordance with the goal of the commercial agency agreement, which is increasing business and customer volume.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

In principle, distribution agreements or intellectual property licence agreements do not have to be communicated to, filed with or registered with a governmental agency, nor is the validity of such agreements subject to governmental approval.

This is, however, without prejudice to the obligation to seek the approval of the competent competition authority (national or the European Commission) in the framework of merger control. If, for instance a merger operation would involve distribution agreements or licences, they must be transmitted to the aforementioned authority for approval (see question 21).

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

Belgian common criminal law contains both anti-bribery and anti-corruption provisions, which have to be respected by both the suppliers and their distribution partners.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

In business-to-business relationships, restrictions to contractual provisions have to be provided for by law. For distribution and agency specifically, one must take into account that (almost all) the legal provisions are of a mandatory nature, meaning that they will apply irrespective of what has been provided for by the parties. This means that contractual provisions contrary to such mandatory legislation will not be enforceable and that certain rules are applicable even in the absence of any provision in this regard (see question 32).

Moreover, the Belgian legislator has provided for specific rules regarding pre-contractual information within the framework of commercial cooperation agreements. It is crucial to seek legal counsel before establishing a distribution network in Belgium, as non-compliance with these rules can result in the nullity of the concerned agreement.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

For exclusive distribution agreements of indefinite term, Belgian law states that as soon as the distribution relationship is implemented, in whole or in part, on the Belgian territory (or a portion thereof), for any matter falling within the scope of the application of mandatory Belgian distribution law, the Belgian courts have jurisdiction and they will apply said mandatory legislation, notwithstanding any contractual provision to the contrary, such as a choice of law clause.

However, these rules are also subject to the application of any relevant rules of international and European law that governs this matter. In practice, a foreign principal will often try to avoid the application of mandatory Belgian law on the unilateral termination of exclusive distribution by providing that foreign law applies to the contract and that foreign courts shall have jurisdiction over any disputes related to the contract. This way, the foreign principal could pursue that the matter will not be referred to a Belgian judge, who will therefore not apply Belgian law.

Mandatory legislation on commercial agency agreements provides that all disputes involving an agent whose principal place of business is located in Belgium shall be subject to Belgian law and to the jurisdiction of the Belgian courts, notwithstanding any contractual provision to the contrary. However, this does not, again, affect the application of international conventions or treaties to which Belgium is a contracting state.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

Belgian commercial agency law stipulates that all disputes involving an agent whose principal place of business is in Belgium shall be subject to the jurisdiction of the Belgian courts, notwithstanding any contractual provisions to the contrary. However, this does not affect the application

of international conventions or treaties to which Belgium is a contracting state.

For exclusive distribution agreements of indefinite term, Belgian law states that as soon as the distribution relationship is implemented, in whole or in part, on the Belgian territory (or a portion thereof), for any matter falling within the scope of the application of mandatory Belgian distribution law, the Belgian courts have jurisdiction, notwithstanding any contractual provision to the contrary, such as a choice of forum clause or an arbitration clause.

However, these rules are also subject to the application of any relevant rules of international and European law that govern this matter. In practice, a foreign principal will often try to avoid the application of mandatory Belgian law on the unilateral termination of exclusive distribution by providing that foreign law applies to the contract and that foreign courts shall have jurisdiction over any disputes related to the contract. This way, the foreign principal could confirm that the matter will not be referred to a Belgian judge, who will therefore not apply Belgian law.

It is also important to note that, under the prevailing case law, arbitration clauses in distribution agreements will only be abided by in Belgian courts if the arbitrators are compelled by the arbitration clause to apply the provisions of the said mandatory legislation in case of an in-scope dispute. A recent judgment opened up some discussion in this regard but it is too early to draw conclusions.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

There are nine commercial courts in Belgium (Brussels Dutch-speaking, Brussels French-speaking, Antwerp, Ghent, Liège, Leuven, Hainaut, Brabant-Wallon and Eupen), which have exclusive jurisdiction to deal with first instance litigation between commercial companies. A judgment can be appealed to one of the five courts of appeal (Brussels, Antwerp, Ghent, Liège and Mons).

Belgium is a party to the European Convention on Human Rights, meaning that all fair trial requirements have to be abided by. There is no restriction on foreign business making use of these courts and procedures.

A court can order a party to disclose the proof that it is considered to be in possession of (article 871 of the Belgian Judicial Code). A mandatory disclosure can also be requested by a party, but will only be granted by the court upon proof of serious, well-defined and concurrent presumptions that the other party has evidence in its possession that might be relevant (article 877 of the Belgian Judicial Code).

Belgian justice is considered relatively cheap and of high quality. However, it can take some time before a final judgment would be handed down.

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40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

Conventional litigation can indeed be side-stepped if parties appeal to an arbitral tribunal. Arbitration can occur both in contractual and in extra-contractual relations between two or more parties. The parties must agree on arbitration through an 'arbitration agreement' or 'arbitration clause' to an agreement.

In practice, arbitration is often more expensive than conventional litigation, but is considered faster and has the advantage of confidentiality.

Also, see question 38 regarding arbitration clauses in distribution agreements.

Canada

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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

Generally, yes. Other than as described in question 4, there is no specific filing or regulatory review process applicable to foreign suppliers looking to establish a business entity or joint venture in Canada. However, it is important to note that, if a subsidiary is established in Canada, certain corporate statutes set out requirements as to the residency of directors pursuant to which at least one director (or 25 per cent of the directors if there are more than four) must be a Canadian resident.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Generally, yes. See question 1, subject to the restrictions described in question 4.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

There are several different vehicles available to foreign suppliers who want to carry on business in Canada, each with varying tax and corporate consequences. A foreign supplier may:

- choose to contract directly with a Canadian distributor without carrying out business in Canada directly;
- opt to appoint a local agent or representative to sell its products in Canada;
- opt to carry on business in Canada using a Canadian branch or division; or
- choose to carry out business in Canada through a federally or provincially incorporated subsidiary or other affiliate.

The preferred choice of vehicle used for an importer owned by a foreign supplier to enter the Canadian market is the incorporation of a Canadian subsidiary or other affiliate. While corporations may be incorporated under Canadian federal law, provinces have also enacted statutes regulating the formation of corporate and other non-corporate entities including corporations, unlimited and limited liability companies and partnerships. Business entities must usually register with the relevant corporate or business registry of each province in which they want to conduct business, pay the prescribed fees and file corporate or business registry forms containing basic information about the business and its ownership and management.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

No substantive restrictions on investment exist, except with respect to very large transactions or investments. Pursuant to the Investment Canada Act, foreign business entities seeking to acquire or establish a Canadian business are required to notify Innovation, Science and Economic Development Canada no later than 30 days following such acquisition or establishment. An onerous and thorough review process applies to non-World Trade Organization investors where the 'asset value' of the acquired Canadian business in 2018 is at least C\$5 million for direct acquisitions or C\$50 million for indirect acquisitions.

However, the C\$5 million threshold will apply to indirect acquisitions where the 'asset value' of the acquired Canadian business represents greater than 50 per cent of the 'asset value' of the global transaction. The review threshold for World Trade Organization investors was raised to an 'enterprise value' of C\$1 billion as of 22 June 2017. Starting on 1 January 2019, this threshold will be indexed annually.

In addition, Canada is a federal system of parliamentary government, and the regulation and administration of certain trans-provincial industries fall within the sphere of federal legislative powers. As for those under provincial jurisdiction, various provinces have regulated certain industries viewed as having particular importance or significance. Thus, several federal and provincial statutes place restrictions on specific industries, such as aviation, collections, engineering, farming, fisheries, banking, trusts and loans, securities, broadcasting, telecommunications, insurance, liquor sales, cannabis and industries that involve the exploitation of Canada's natural resources. Depending on the products being distributed, these restrictions may affect international distribution arrangements where the foreign supplier has a direct or indirect presence in Canada.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

Generally, yes. Please refer to questions 1 and 3, subject to the restrictions described in question 4.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

Depending on the business structure selected by a foreign supplier wanting to sell goods in Canada, different taxes may apply on its income.

Canadian residents are taxed on their worldwide income, whereas non-residents may be taxed in Canada when they sell taxable property or earn employment income in Canada. If the supplier carries on business in Canada through a fixed place of business or permanent establishment, any income derived in respect thereof will generally qualify as 'business income' that is taxable in Canada on a net income basis.

Canada has entered into taxation-recognition treaties with a large number of countries; if the foreign supplier is from a treaty country, it will generally be exempt as long as it does not carry on its activities through a 'permanent establishment' in Canada.

The income of a non-resident supplier carrying on business through a 'branch'-type of operation in Canada will typically be subject to a 'branch tax', which is the income tax that applies when a non-resident corporation carries on a business in Canada through a 'branch' (ie, by itself having offices, employees, files or other aspects of a permanent establishment in Canada) as opposed to a Canadian subsidiary. The base rate for branch tax is 25 per cent of Canadian taxable income earned through the branch in Canada but may be reduced by tax treaties, if applicable.

If a foreign supplier appoints a local agent or representative to sell its products in Canada, income earned by the supplier through sales originating from the agent may, depending on the agent's commission or fee structure, be characterised as passive income and subject in Canada to a withholding tax. If so, the agent would be responsible for

withholding the tax and remitting amounts to Canadian tax authorities. The standard withholding tax rate of 25 per cent under Canadian income tax legislation is often reduced to 10 per cent by tax treaties, if applicable.

Canadian withholding tax on passive income would not be payable if a subsidiary or other affiliate is established in Canada. Nonetheless, dividends paid to its parent would be subject to a withholding tax of 25 per cent – this rate can be reduced to as low as 5 per cent by tax treaties, if applicable.

In conclusion, a thorough review of all relevant Canadian legislation pertaining to each structure and a careful evaluation of the effect of tax treaties entered into and ratified by Canada with the foreign supplier's jurisdiction, on a case-by-case basis, is strongly advised.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

There are several options available to suppliers for establishing a distribution structure. The most common structures and their principal features are outlined below:

- direct distribution, where the foreign supplier uses a Canadian subsidiary or its own employees to sell goods in Canada – see questions 1 to 6;
- independent agents and representatives, where the supplier relies on an agent or representative to originate sales of goods in Canada and pays them a commission on the goods sold to customers in Canada;
- trademark licensing, where the supplier gives a Canadian entity a licence entitling it to use its intellectual property rights to manufacture and distribute goods for the Canadian market; franchises, which give rise to special considerations given that several Canadian provinces (namely, Ontario, British Columbia, Alberta, Prince Edward Island, New Brunswick and Manitoba), have enacted franchise-specific legislation (the Franchise Acts), under which the term 'franchise' is broadly defined – as a result, a variety of other contractual relationships, including distribution, agency and trademark licensing agreements, may possibly be encompassed;
- prior to formalising any particular distribution, agency or trademark licensing arrangement for Canada, parties should carefully examine provincial legislation and consider whether they would be subject to franchise legislation, which entails a duty of disclosure and fair dealing and may give rise to additional requirements for a supplier that are not generally intended in the context of a distribution, agency or trademark licensing arrangement;
- private label, where a Canadian distributor sells the foreign supplier's products under its own name and trademark. This allows the foreign supplier to sell products in Canada while having the benefit of being recognised under local brand name, but generally provides very little control by the supplier; and
- joint ventures, where the supplier relies on a local distribution partner that is owned in part by the supplier.

Each of the above can be established by a contractual arrangement and the parties are generally free to determine their respective rights and obligations under the agreement, subject to certain restrictions discussed in question 8.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

In general, parties to a distribution or agency agreement are free to establish the terms of their relationship by contract, subject to the expansive definition of a 'franchise' under the Franchise Acts. In addition, as mentioned in question 4, certain industries are specifically regulated by federal or provincial law.

As a result, care should be exercised when structuring an arrangement that may fall within the ambit of the Franchise Acts or that, by its nature, may be subject to restrictions in a regulated industry.

Additional restrictions arise as a result of competition laws, as discussed in greater detail in questions 14 to 22.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

The parties to a distribution or agency agreement can provide for termination without cause in the contract. If the contract stipulates that such a termination can occur without notice and with immediate effect, such a stipulation will generally be enforced as long as it is provided for in express and unequivocal terms. If the contract is silent as to the requirement to provide notice in the event of a termination without cause, the length of the notice period will vary according to the factors described in question 10.

No specific cause is required to terminate a distribution or agency contract. If the contract is silent as to the possibility of terminating without cause, it is generally possible to terminate the arrangement upon reasonable notice. (The factors for determining what constitutes reasonable notice are discussed in question 10.)

As for termination with cause, the parties may establish, by contract, occurrences that constitute events of default giving rise to termination. Where the contract is silent, Canadian courts have generally required evidence of a fundamental breach (or, in Quebec, a serious or material breach), in order to find cause for termination; short of establishing a cause, the provision of reasonable notice would be necessary in order to lawfully terminate the relationship. In addition, Quebec law requires that termination rights always be exercised in good faith – refer to question 33 for a more fulsome discussion on good faith in Canadian contracts.

If the contract is for a fixed term, it would naturally expire at the end of the term and there would not generally be any compensation payable at that time. However, if the parties choose to continue their relationship after the end of the term, it may constitute an implicit renewal or an extension of the contract for an indeterminate term.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

There are no statutory provisions governing compensation upon termination for distribution or agency agreements. In general, courts have found that no compensation is due if reasonable notice has been given and compensation equivalent to reasonable notice is typically granted where a contract is terminated without notice. The amount of the indemnity, which effectively replaces the notice period, would be estimated based on past profits, and would take into account factors such as the length of the relationship, the nature of the relationship (including whether it was exclusive), industry practice, investments made by the distributor for purposes of the agreement, and the time it would take the distributor to obtain a similar source of income from an alternate supplier.

Parties can agree to pre-establish a liquidated damages clause or, under the civil law of Quebec, a termination penalty, and such a contractual provision will be enforceable unless it is deemed unreasonable by the courts.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

Generally, yes. If the contract is silent with respect to transfers or changes of control, then it is generally assumed that such an operation is permitted without the supplier's consent unless the arrangement constitutes an *intuitu personae* contract.

However, in Quebec, if the contract does not provide whether an assignment or transfer may occur without the other party's consent, their consent would generally be required.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

Confidentiality agreements are normally enforceable under Canadian law, subject to certain exceptions such as being compelled to disclose under law or in the course of legal proceedings. Under Quebec law, disclosure of confidential information is also permitted for public health or safety reasons.

Information that is publicly available or generic cannot be regarded as confidential. Trade secrets that meet the jurisprudential criteria of being known by only a few people within a given business and are treated as such within said business would be protected irrespective of contractual provisions. However, it is generally prudent to include a contractual provision regarding restrictions on the use of information acquired in the course of the distribution or agency agreement, especially where it could be used by one party to the detriment of the other.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

In general, yes, subject to restrictions established by the Competition Act (Canada), which are outlined in further detail in questions 14 et seq.

Restrictions on distributing competing products during the term of the relationship are generally enforceable. However, restrictions on competition that extend beyond the term of the agreement must be reasonable and coherent with the contract's purpose, and are read restrictively by Canadian courts. Non-competition clauses must be limited with regards to term, geographic area and activities restricted, the whole in accordance with what is necessary to protect the supplier's or principal's legitimate interests, failing which the provision risks not being enforced in any aspect. Moreover, a supplier or principal would not generally be able to rely on such a restriction if the agreement is terminated without cause by them or as a result of their conduct.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

Price maintenance is a reviewable trade practice under Canada's Competition Act. The threshold for enforcement authorities to apply sanctions on the basis of price maintenance requires that the supplier's conduct be likely to adversely affect competition. It is common for suppliers to provide suggested retail prices on packaging and labels.

The Competition Tribunal may make orders for a reviewable trade practice to cease, or compel a business to accept a given customer or order on reasonable trade terms. Fines may also be applicable if conduct is found to lessen competition, and compensation may be payable to private parties who have been granted leave by the Tribunal to bring a claim.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

Minimum advertised price policies are common and, while they constitute reviewable trade practices under the Competition Act, they are only viewed as problematic where there is an adverse effect on competition.

Minimum advertised price policies must be established unilaterally by the supplier and must be uniformly enforced. They should also specifically allow products to be sold at prices lower than the minimum advertised price as this provides distributors and agents with the requisite flexibility to offer on-location discounts, coupons and other rebates.

Please see question 20 for a discussion on the rules applicable to refusals to deal.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

Generally, yes. The parties are free to establish their agreed terms of sale in their agreement, including pricing preferences, subject to certain restrictions outlined in question 17.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

Price discrimination and promotional allowances (whether through discounts, rebates, allowances, price concessions or other advantages), are reviewable trade practices under the Competition Act but would generally only be problematic if they significantly lessen competition.

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

Providing for an exclusive territory or other market restrictions in a distribution or agency agreement would not be prohibited, but would be subject to oversight by competition authorities. Unless the restrictions substantially lessen competition, they would not be enjoined. For details with respect to the consequences of failing to comply with restrictions in respect of such practices, see question 14.

It is generally permissible for a supplier to reserve the rights to distribute products in certain territories or through certain channels or to specific types of customers (for example, by reserving the rights for online selling), as long as the arrangement does not substantially lessen competition.

The distinction between active and passive sales efforts, as it is understood in Europe, is generally not applicable under Canadian law.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

As is the case with reselling generally, restricting or prohibiting e-commerce sales altogether or in respect of an exclusive territory in a distribution or agency agreement would not be prohibited, subject to restrictions implemented by the Competition Act (Canada). The anti-competitive restraints provided by the Act are applicable to both online and brick-and-mortar retailers. The same principles discussed in question 18 would therefore apply to territorial restrictions on e-commerce sales.

Accordingly, a supplier may entirely prohibit or otherwise limit e-commerce sales by its distribution partners to a given territory or otherwise, so long as these restrictions do not adversely affect competition. Subject only to the foregoing anticompetitive concerns, the parties are free to establish reporting obligations, and the consequences of any failure to comply with (or deviations from) the contractually established territorial rights, that comply with legal principles applicable in the relevant province.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

Refusal to deal is a reviewable trade practice under the Competition Act and would give rise to enforcement only where the practice substantially lessens competition. A supplier is otherwise free to decide who it chooses to do business with; restrictions on a distributor's resale rights are generally permissible, as discussed in question 18.

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

In practice, without significant market power or concentration, it is unlikely that a typical distribution arrangement would trigger oversight of this nature.

Mergers and other transactions may be subject to review where they 'prevent or lessen competition substantially' within a given industry. Indicators for reaching this threshold include considering whether an entity holds significant market share, whether there are significant barriers to entry in a given market, the availability of acceptable substitutes, effective remaining competition, and the extent of foreign competition. Competition authorities also consider whether the operation generates efficiencies that offset the anticompetitive effect to ascertain the overall effect on competition.

Certain types of joint ventures or strategic alliances may be subject to review if they are likely to substantially lessen or prevent competition. Vertical arrangements between suppliers and their customers are assessed on the same basis.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

In addition to the restrictions discussed in questions 14 to 20, exclusive dealing is a reviewable trade practice under the Competition Act, but conduct of this nature would not generally be subject to sanctions unless requiring a distributor to purchase its products exclusively from a given supplier is likely to have a significant adverse impact on competition.

Enforcement and remedies are also discussed in questions 14 to 20.

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

The sale of grey market products will not generally constitute trademark infringement under Canadian law. However, where a Canadian company is the registered owner of a Canadian trademark, and is distinct from its international supplier or manufacturer, it would be in a position to rely on the provisions of the Trade-marks Act (Canada) to contest parallel imports and the distribution of grey goods, as demonstrated in the 'Update and trends' section.

A distributor or agent would not have any recourse where the trademark is owned by a foreign entity from which originates both the legitimately imported grey market goods and the goods destined to be sold by the distributor or agent. A passing-off action may occasionally be successful where the grey market goods do not meet Canadian safety or labelling requirements.

As a practical matter, suppliers who sell goods to a wholly owned subsidiary or other affiliate for distribution in Canada should ensure that the local subsidiary or affiliate is the owner of the trademark in Canada. Ensuring that the product is specifically designed and labelled for the Canadian market will also facilitate the preservation of rights against parallel imports.

Holders of a copyright (for example, in a brand logo) are also afforded a certain level of protection against parallel imports under the Copyright Act (Canada). To qualify for this supplemental protection, it is recommended that the Canadian distributor be assigned the copyright in Canada rather than being given an exclusive licence to use it; if the distributor is not an affiliate of the supplier, it may be preferable to allow for the copyright assignment to be reversed at the end of the contract.

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

In Canada, the federal government generally regulates advertisement through the Competition Act, which prohibits any advertisement that is false or misleading in a material respect. The materiality of the representation is considered in the light of whether it may influence a consumer to buy or use the product or service advertised, based on the general impression conveyed by an advertisement, in addition to its literal meaning.

Advertising Standards Canada administers the Canadian Code of Advertising Standards, which sets out criteria for acceptable

advertising and guidance on inaccurate, deceptive or otherwise misleading claims, statements or representations, as well as price claims, comparative advertising and testimonials.

Most Canadian provinces also have legislation regarding consumer protection and business practices, many of which include prohibitions on false, misleading or deceptive representations made to consumers. Certain such legislation also contains specific prohibitions, such as restrictions on using representations that products confer any particular benefit or standard of quality, and restrictions on inaccurately advertising price advantages. Certain provincial legislation provides for more serious protections with respect to the unfair practice of making unconscionable representations.

As for the responsibility for marketing and advertising in a distribution or agency relationship, the supplier and its contractual counterpart may determine their respective contributions by contract.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

The types of protections available depend largely on the nature of the intellectual property rights in question, but most types of intellectual property benefit from the same types of safeguards as are commonly recognised internationally, and may be exercised by a supplier against both distribution partners and third parties.

Trademarks

Trademarks are protected under the Trade-marks Act. Distinctiveness is central to the definition and a trademark need not be registered to be valid, or even licensed, in Canada. Registration with the Canadian Intellectual Property Office has the advantage of providing nationwide protection of the registered trademark, as opposed to limited protection in geographical areas where a common law mark (ie, an unregistered mark) is known.

In the distribution and agency context, remedies available to a supplier in respect of its distribution partner (for example, following a breach of exclusive use clauses or the use of a confusing trademark) range from injunctive remedies to passing-off actions. These remedies are also available for infringement or other recognised violations by third parties.

Patents

Innovations that are new, useful and inventive can be protected under the Patent Act (Canada). Patented innovations must be registered with the Canadian Intellectual Property Office in order to be afforded protection.

Unless otherwise contractually stipulated, the Patent Act provides that a person who infringes a patent is liable to the patentee and to all persons claiming under the patentee for acts of infringement. Injunctive relief and damage claims would be available, and may be instituted against distribution partners and third parties who engage in prohibited practices in respect of patented concepts.

Copyright

Copyright is protected under the Copyright Act. Protection is extended, irrespective of registration, for all original works produced in any country that is a signatory of the Berne Convention. However, registration with the Canadian Intellectual Property Office is possible.

Remedies for copyright infringement under the Copyright Act include damages, lost profits, and injunctions prohibiting distribution or ordering the destruction of infringing goods. Actions can be brought by the copyright owner against distribution partners or any third parties.

Know-how and trade secrets

There is no statutory protection of know-how or trade secrets in Canada.

Common law affords protection to trade secrets that are known by only a few people within a given business and are treated as such within said business. Parties must also rely on common law tort and contractual undertakings to protect know-how from unauthorised disclosure or use.

Accordingly, the nature of the confidential information that a supplier wishes to protect, as well as the legal consequences arising as a result of its dissemination, should be clearly identified by the contracting

parties in their agreement. In the event that this tort occurs, injunctive relief and damages may be sought by a supplier against a distributor or any third party before the provincial courts with competent authority.

Technology transfer agreements

Technology transfer agreements are not generally used in the distribution and agency context.

26 What consumer protection laws are relevant to a supplier or distributor?

In addition to the advertising rules provided in the Competition Act (described in question 24) and the requirements of the Consumer Product Safety Act (discussed in question 27), most Canadian provinces have legislation regarding consumer protection or business practices or both, as discussed in question 24.

Additionally, rules relating to warranties and vendor liability may be relevant in the consumer context, as discussed in question 28.

Of importance with respect to online sales, certain provinces in Canada impose specific formalities in respect of distance (or remote) contracts, where a consumer contracts without being in the physical presence of a merchant.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

The Consumer Product Safety Act (Canada) (CCPSA) grants Health Canada, the federal ministry charged with public health matters, sweeping powers to issue mandatory product recalls and require product safety tests. The CCPSA applies where products are usually obtained by an individual for non-commercial purposes and imposes a general threshold of 'danger to human health and safety', which is evaluated on the basis of whether an existing or potential hazard is posed by a product during its normal use and can cause death or have an adverse effect on an individual's health in the short or long term.

In case of an incident, a manufacturer or distributor can either voluntarily issue a product recall or the recall may be ordered by Health Canada. Incidents include: occurrences that caused or could have caused death or injury; situations where a dangerous defect is noticed; situations where an incorrect, insufficient or non-existent label creates a risk of death or injury; and situations where another domestic or foreign public body initiates a recall. If a product is subject to a recall, the manufacturer (or, if the manufacturer is foreign, the importer) must provide Health Canada with information regarding the incident and file a mandatory incident report.

Specific risks relating to particular classes of products, such as candles, glass items, mattresses, children's jewellery and sleepwear, toys, food, drugs, cosmetics, medical devices, tyres, carriages and strollers, cribs, cradles and bassinets, helmets, car seats, residential smoke detectors, firearms and ammunition, are further dealt with in detailed regulations.

The parties to a distribution or agency arrangement may determine contractually who is responsible for the costs associated with recalls and for carrying out any applicable formalities. However, it should be noted that Health Canada also has the power to initiate a recall under the CCPSA; as a result, the allocation of responsibility established by the parties may be overridden in practice, though contractual indemnities would still apply between the parties.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

The supplier and distributor may contractually allocate among themselves the risks relating to products, including with respect to warranties. Products may usually be sold by a supplier to a distributor without any warranty at all. However, the extent to which implied warranties may be disclaimed varies by province and certain exceptions apply. For example, in Quebec, a seller may not be able to disclaim damages if it has knowledge pertaining to deficiencies relating to the quality of its products, if it commits gross fault or negligence, or where bodily or moral harm occur. In addition, downstream customers other than a first-hand purchaser could have recourse against the manufacturer

and other members of the distribution chain if a product suffers from a safety defect.

With respect to consumer warranties, most Canadian provinces have 'sales of goods' legislation that regulate them and prohibit limiting such warranties contractually. In Quebec, strict liability applies to product defects under consumer protection law, and neither the distributor nor the supplier may limit consumer warranties; moreover, the benefit of a consumer warranty cannot be waived by a consumer.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

In Canada, the federal Personal Information Protection and Electronic Documents Act (PIPEDA) contains significant protections for individuals whose personal information may be collected, used and shared by people or entities with which they have dealings. PIPEDA requires that individuals provide informed consent before their personal information is processed and shared and the individual concerned must be informed of the projected uses of the data in advance. In Canada, the law also requires disclosure where data may be processed or stored in other countries or by entities other than the one collecting the data, whether domestically or abroad, even if such processing or storage is done on behalf of the entity collecting the data. Additionally, in light of recent amendments to PIPEDA, organisations subject thereto may, in certain circumstances, be required to report and maintain records of security breaches involving personal information under their control.

One of the purposes of PIPEDA's adoption was to align Canadian legislation with the European Union's strict privacy requirements. However, the federal government has since passed the Anti-terrorism Act 2015, which grants the government broad access to personal information for national security reasons. As such, in the aftermath of the *Maximillian Schrems v Data Commissioner* (C-362/14, 2015) decision, it may be unwise to assume that Canadian legislation continues to satisfy the EU's highly protective privacy standards, and that the transfer of data between the EU and Canada remains unaffected, especially in light of the enactment of the EU General Data Protection Regulation in 2018. The same attitude should be adopted in light of the new Privacy Shield regime between the EU and the US. While Canadian privacy legislation has not been directly affected by its implementation, Canadian businesses that store or process personal information about EU citizens should be mindful of how the principles in the Privacy Shield agreement may affect their practices.

The provinces of Quebec, Alberta and British Columbia have enacted privacy legislation that extends similar protections to individuals and applies to private sector entities under provincial jurisdiction. Under Quebec law, persons who collect personal information must refrain from transferring this information to jurisdictions where it would not be afforded the same protections as those required under Quebec privacy law.

The parties to a distribution or agency agreement may determine who 'owns' the information collected from customers and end users (although Canadian privacy law does not consider that data is in fact owned by those who collect, transmit or use it), but the restrictions described above will apply to all of those who collect, use, share and store such information.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

In general, the parties are free to govern their relationship by contract, including granting the supplier approval rights over the individuals who manage the distribution partner's business or termination rights as a result of reasonably objective management failures to comply with the stated objectives or obligations of the distribution relationship. However, this may not be the case with distribution arrangements subject to Franchise Acts or in industries that are subject to certain specific regulations and legislation – see questions 7 and 8.

Without specific contractual provisions producing the desired effect, a supplier's dissatisfaction with the distributor's management would generally not be considered sufficient cause to terminate a distribution relationship without notice.

Update and trends

While it remains unsettled as to whether Canadian trademark law is the proper vehicle for contesting parallel imports, the Ontario Court of Appeal recently upheld certain settlement agreements prohibiting the sale of grey market candy products in Canada by an unauthorised third-party distributor. This case involved Mars Canada Inc (Mars Canada), the registered owner of the Mars candy brand in Canada, and Bemco Cash & Carry Inc (Bemco), an unauthorised distributor that was importing Mars products from the United States and selling them in Canada at a lower price than that offered by Mars Canada. In 2006, Mars Canada discovered Bemco's grey market distribution into Canada and accordingly filed an action against Bemco. Following lengthy negotiations, the parties reached a settlement agreement whereby Bemco agreed to cease importing and selling Mars products in Canada without Mars Canada's consent and revealed the identity of its grey market supplier, GPAE Trading Corp (GPAE). Mars Canada then concluded a parallel settlement agreement with GPAE.

The legality of these settlement agreements was later challenged and upheld by the Ontario Court of Appeal, despite Bemco's and GPAE's contention that such agreements were in 'restraint of trade' and therefore in breach of Canadian competition laws. The court concluded that, although the settlement agreements might be

considered in 'restraint of trade' and did not fall within any statutory exceptions, such agreements were reasonable in light of the interests of the parties and the interests of the public. Indeed, the purpose of the settlement agreements was to protect Mars Canada's trademark rights as well as to resolve ongoing litigation. Moreover, the court stated that Mars Canada was entitled to enforce its proprietary interests as a brand owner and authorised dealer of the Mars candy products in Canada by bringing suit against Bemco and GPAE. The court also took note of the fact that the products imported by Bemco did not comply with Canadian packaging and labelling requirements. For these reasons, the court concluded that the settlement agreements were reasonable and should be upheld.

This decision suggests that manufacturers may be able to exclude grey-market merchandise in Canada through the use of trademark law, as is the case in the United States. This decision also confirms that having a Canadian subsidiary distinct from its international supplier and manufacturer as the registered owner of the Canadian trademark is helpful in counteracting the effects of grey market distribution channels. Furthermore, this decision also serves as a reminder that distributors will be unable to escape scrutiny if their grey-market products do not comply with Canadian packaging and labelling laws.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

Each Canadian province has enacted its own health and safety, employment standards and labour relations legislation. Accordingly, provincial laws and regulations govern most matters relating to labour law.

Depending on the nature of the relationship, there is a risk that a distributor or agent may be considered an employee, in which case the supplier would be subject to mandatory rules applicable to minimum wage rates, overtime wages, vacation and leave compensation, hours of work, severance and notice periods, as well as union certification and collective bargaining laws, all of which vary greatly by province and industry.

In order to mitigate these risks, the parties may specify by contract that they are independent contractors and cannot be responsible for each other's actions, including in connection with labour and employment matters.

To avoid any unintended characterisations, care must be taken to ensure that each distribution partner operates as a distinct and truly independent entity from a supplier (ie, no common control or direction emanating from the supplier that is greater than that which typically characterises the distribution or principal-agent relationship) so as to be considered a separate employer for labour union certification and collective-bargaining purposes.

32 Is the payment of commission to a commercial agent regulated?

The parties are generally free to establish the agent's compensation by contract. As noted in question 6, to the extent that commissions attract withholding tax, the agent will be responsible for withholding the applicable amounts and remitting them to the tax authorities in Canada on behalf of the principal.

33 What good faith and fair dealing requirements apply to distribution relationships?

The Supreme Court of Canada has found that there is an inherent duty for parties to honestly perform their contractual obligations, and many common law courts have held that an implicit obligation of good faith exists in contractual dealings. A perhaps more fulsome obligation exists under articles 6, 7 and 1375 of the Civil Code of Quebec, which imposes a duty on all parties to conduct themselves in good faith in all contractual dealings, including at the precontractual stage.

Additionally, the Franchise Acts, which may apply to certain types of distribution agreements (see question 7), include an explicit duty of good faith and fair dealing during the term of the contractual relationship.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

No legislation directly governs international distribution agreements or expressly requires the registration of a distribution agreement with a foreign national with any authorities in Canada, subject to the observations in question 7.

There is no requirement to register a trademark licence and there is no clear adverse effect of failing to do so in a timely manner.

Under the Copyright Act, a copyright licence must be granted in writing and must be signed by the owner of the right in respect of which the licence is granted or by its duly authorised agent. The grant of a copyright licence may be registered, and the rights of any registered licensee will take priority, without notice, over any prior unregistered licensees.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

Bribery and corruption of public officials are crimes in Canada under the Criminal Code (Canada), for both the corruptor and the corrupted official. In addition, the Corruption of Foreign Public Officials Act (Canada) applies to acts of corruption or bribery committed by Canadian persons outside of Canada. Charges may also extend to those who aid or abet offenders.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

Most of the restrictions and prohibited practices in respect of distribution and agency relationships have been addressed in specific questions above. There are no mandatory provisions or automatic inclusions in contracts and the parties are generally free to set out the terms of their agreement by contract.

In certain cases, courts enforcing an agreement in Canada will be required to apply mandatory provisions of local law. Overriding a contract by reason of mandatory local law would generally apply only where either the contract or the parties' conduct is inconsistent with public policy, for which the threshold is no lower in Canada than in other jurisdictions with sophisticated legal systems. Many of the rules that could be considered mandatory in Canada have been discussed in detail previously, such as limitations on restrictive covenants, competition issues, limitations of liability, privacy laws and criminal matters.

Governing law and choice of forum**37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?**

The parties are free to choose the laws that will govern their relationship. All Canadian provinces permit the selection of a foreign governing law as long as doing so is not considered to be in fraud of the domestic law, subject to the application of laws or provisions of public order in Canada as mentioned in question 36.

Canada is party to numerous international treaties such as the Vienna Convention on the International Sale of Goods; where the selected or applicable law is that of Canada, the foregoing Convention finds automatic application unless expressly set aside by the parties in their contract.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

The parties may elect to submit to the courts or arbitration tribunals of any jurisdiction, subject to the observations in question 37.

Choice of forum clauses are generally enforced by Canadian courts, thus making it possible for the parties to select a non-Canadian court to resolve disputes or claims arising from their agreement, even where they are related to occurrences in Canada. In addition, mediation and arbitration are viable and recognised mechanisms of dispute resolution across Canada.

A final monetary and conclusive judgment on the merits from a foreign court is usually enforced by Canadian courts. Certain provinces, such as British Columbia and Ontario, have enacted legislation that provides a simplified procedure for registering and enforcing foreign judgments and arbitration awards. Arbitration awards are readily recognised throughout the country as Canada is party to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

In civil matters, provincial courts generally have jurisdiction except for those matters that are specifically reserved to the federal judiciary (such as intellectual property, bankruptcy, trade and commerce). Injunctive relief is available in all provinces and may be granted on an interim, interlocutory or permanent basis. The right to seek such relief is always within the discretion of the court and cannot be waived.

There is no legal discrimination or heightened level of legal requirements for foreign businesses to adjudicate disputes before courts in Canada. Nevertheless, foreign businesses may be subject to different mandatory costs than would domestic businesses.

The discovery process is an integral part of litigation in Canada and is subject to comprehensive rules of procedure that generally require disclosure of documents and provide for compulsory verbal testimony, each to the extent required to establish the allegations and defences put forth in a given case. There are certain exceptions, such as documents or other information that are subject to attorney-client privilege; however, judicial authorities tend to otherwise allow and encourage submissions and fulsome disclosures with a view to seeking transparency and avoiding any loss of rights to the parties involved in a dispute.

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

The parties may expressly and contractually agree to arbitrate their disputes in the venue of their choosing to the exclusion of Canadian courts. Even in the presence of an unequivocal arbitration clause, certain remedies (such as injunctive relief and other extraordinary recourses) may nonetheless be sought before the courts.

The principal advantages and disadvantages of arbitration for foreign suppliers in Canada are essentially the same as for local suppliers. Arbitration has the main advantage of being confidential. Disputes between suppliers and distributors, or agents, do not become a matter of public record as would be the case with litigation in the judicial system. In addition, arbitration gives the parties a level of control that they may not otherwise have over some aspects of the dispute, such as choice of venue and forum and the selection of an arbitrator with expertise in distribution and agency issues or the relevant technical or specialised fields. Arbitration agreements are final, reliable and not open to appeal; Canadian courts have generally refrained from intervening in such decisions. Finally, arbitration tends to be faster and cheaper than litigation, at least in theory.

As for its disadvantages, arbitration, like litigation, can become bogged down procedurally, diminishing the cost and time savings that often motivate its use. The lack of ability to appeal heightens risk for the parties that have no recourse against an unfavourable decision. Some also argue that arbitration clauses that preclude access to the judicial system will prevent the use of proceedings such as injunctive or other equitable relief that can be obtained quickly to effectively end a breach of contract.



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China

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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

Under the current regulatory environment, a foreign supplier may establish its own entity (wholly owned) to import and distribute its products in China, subject to some exceptions such as certain audiovisual work, agricultural products and gasoline where joint venture arrangements remain as the requisite structure to attain approval. There are some product categories that are still not open to foreign investors such as genetic testing equipment and military products, and local importers and distributors have to be engaged for importing these products.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

As mentioned, a foreign supplier may enter into a joint ownership arrangement with a local company or importer for the importation of its products, except products that are still not open to local trading by foreign investors. There are two major joint ownership structures: joint ventures in China and limited liability companies invested by the parties in China. For a joint venture in China, there is a choice of two types: equity joint ventures and contractual joint ventures. For an equity joint venture, each party must make a cash or permitted contribution and share the profits in proportion to its subscribed percentage of the venture's registered capital. For a contractual joint venture, the parties may agree in the joint venture contract that profits will not be distributed in proportion to the subscribed percentage of the venture's registered capital. Parties can invest in limited liability companies with a direct shareholding structure to set up holding companies outside China (using locations such as Hong Kong owing to certain tax considerations) and then the Chinese entity can be placed under such offshore holding structure.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

Unless it is required by law that a joint venture be established, from a corporate management perspective, a wholly foreign-owned enterprise (WFOE) is generally the preferred type of business vehicle for a foreign supplier to import and distribute its own products. A WFOE will be incorporated as a limited liability company in which the foreign supplier is the only shareholder. The establishment, operation and termination of the WFOE is governed by the Company Law of the People's Republic of China (PRC) and the Law of the PRC on Foreign-invested Enterprises. There are different local approval procedures for certain businesses.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

The Chinese regulatory environment is more focused on the regulation of business than on the ownership of business entities, and the scope of business of a business entity is specifically defined in the corporate formation documents. In essence, conducting any business beyond the approved scope of business is illegal. Foreign investors are required to follow the Catalogue of Industries for Guiding Foreign Investment (Catalogue) to verify whether the proposed business is restricted under

national and local regulations. In the Catalogue all industries are divided into three groups:

- encouraged industries;
- restricted industries; and
- prohibited industries.

Foreign investors are not allowed to conduct business, or invest, in prohibited industries and are subject to several restrictions for investing in restricted industries. The Catalogue may be subject to changes by the government from time to time.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

See question 3.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

The major relevant taxes are corporate income tax, value added tax and customs duties. China also follows the Organisation for Economic Co-operation and Development model on the issue of transfer pricing. The tax authority in China has been using the industrial average profit margin generated from its database to determine whether the assessable income should be adjusted due to certain transfer pricing arrangements between related companies.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

Various distribution structures are available in China, including the typical structures of distributorship, commission agency, franchise, trademark licence and joint ventures. Apart from the usual business considerations such as whether the model can achieve better penetration into the market and serve the objectives of the brand owner, tax issues and actual logistic arrangements are also crucial in determining whether a certain structure is preferred. For example, it is common to use local agencies for importing cosmetic products due to certain testing procedures of the China Food and Drug Administration, and the distributors are supplied through such local agencies.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

Generally, the Contract Law of the PRC governs the relationship. There is no specific government agency regulating the distribution aspect, provided that in the context of franchising, the Ministry of Commerce is the regulatory authority that oversees compliance pursuant to the franchise laws and regulations such as the Regulations of Administration of Commercial Franchising. Recently, the government released a series of national standards for different sectors stipulating the necessary standards for management of different contractual relationships. However, the legal position of these national standards has not yet been defined.

- 9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?**

The Contract Law of the PRC does not restrict the supplier's contractual rights to terminate a distribution relationship without cause. The contractual provisions regarding termination are usually descriptive and elaborate in contracts with Chinese parties, because some common concepts in other jurisdictions, such as time sensitivity, do not exist under Chinese law.

- 10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?**

The Contract Law of the PRC does not require the brand owner to provide a mandatory compensation or an indemnity at the termination of the distribution or similar relationship. There is no requirement under the law to compensate the distributor for the goodwill established by the distributor.

- 11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?**

It is common to have change of control provisions in distribution or agency contracts enabling termination of the agreement in the event of transfer of ownership of the distributor or agent to a third party, and so far there is no specific judicial precedent prohibiting the enforcement of such contractual provisions.

Regulation of the distribution relationship

- 12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?**

Confidentiality provisions in distribution agreements are generally enforced contractually and there are also statutory protections under the Anti-Unfair Competition Law of the PRC. However, the usual challenges relate to the mechanism implemented to protect the confidential nature of the information involved (eg, document marking, restrictions to access, etc) and it is necessary to devise a system to protect the confidential information. The Anti-Unfair Competition Law of the PRC (2017 Revision) abolished the previous requirement that confidential information should be of practical value, and the coverage of confidential information has expanded.

- 13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?**

So far the judicial precedents have not shown a very systematic approach towards the determination of enforceability of non-compete provisions. Non-compete provisions are generally enforceable during the term of the distribution relationship. It is generally agreed that non-compete provisions are enforceable if the restricted period is not excessively long (eg, after two years for the original distribution territory is generally acceptable). In determination of the reasonableness of certain restrictions, the general 'fair and reasonable' test, which is relatively vague, is adopted.

- 14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?**

Generally, distributors can be required to follow the supplier's pricing policy. However, under the Anti-Monopoly Law of the PRC, price-fixing arrangements, to monopolise the market, between the supplier and distributors are prohibited, and there are other restrictions mentioned below.

- 15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?**

Minimum advertised price policies that only regulate the advertised resale prices without restricting the actual resale prices to be negotiated by the distributors and the customers are common nowadays, but such provisions remain relatively untested. It is necessary to mention that a supplier may violate the Anti-Monopoly Law of the PRC if it enters into an arrangement with a distributor to fix resale prices or set minimum resale prices to achieve market monopoly. It is advisable to make the termination provisions related to violation of the pricing policy and minimum advertised price policy more detailed.

- 16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?**

The general belief is that this type of 'most-favoured customer' provision is enforceable. However, the Anti-Monopoly Law of the PRC prohibits a distributor from abusing its dominant position in the market to secure certain trading conditions that restrict market entry by other parties.

- 17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?**

The law generally does not intervene in the freedom of dealings between the parties on pricing issues. The exception is that under the Anti-Monopoly Law of the PRC, a supplier who is in a dominant position in the market is not allowed to offer different transactional terms and conditions (eg, sale prices) to customers (which means the distributor in the present context) with the same background without proper reason. There is no statutory definition of 'customers who are of the same background', and the court has wide discretion to determine who may be in breach of this law.

- 18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?**

It is common to agree on exclusive territory for a particular distributor, and the contractual provisions remain decisive in determining how to define the territories and markets. The law so far has not provided sufficient guidance on construing the contractual provisions of active sales and passive sales that are not actively solicited, but which are heavily litigated in other jurisdictions.

- 19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?**

It is common that a supplier restricts or prohibits e-commerce sales by its distribution partners in China, as e-commerce distribution rights are normally separately granted. Whether restrictions as to the use of e-commerce intermediaries exist is a matter of negotiation between the parties but the engagement of e-commerce intermediaries is a growing phenomenon in the past few years. The provisions on territorial limitation as to distribution activities with enhanced technological requirements are seen in most of the distribution agreements. A supplier may require that its distribution partners, or e-commerce intermediaries, do not sell products outside the assigned territory. Under the highly computerised environment of e-commerce, it is usual for suppliers to request their distribution partners to provide more reports as to sales by territory, and some distribution systems have a specific fee or 'invasion fee' for sales out of its authorised territory.

- 20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?**

The Anti-Monopoly Law of the PRC prohibits businesses that are in a dominant position in the market from refusing to deal with particular

customers, or from restricting their distributors from dealing with certain parties, without proper reason. There is no statutory definition for 'proper reason', which is subject to the determination by the courts at their discretion on a case-by-case basis. However, if there is no abuse of a dominant position, the prohibition should not be relevant, and the supplier is free to devise a policy on selection of customers.

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

Under the Anti-Monopoly Law of the PRC, a merger or common control of shareholdings of different competitors, entering into arrangements for control of different competitors, may lead to a concentration situation, and such a situation is subject to reporting and approval requirements. There are further rules defining what reportable situations are, some examples of which are as follows:

- if the annual global sales figure for the concentration is more than 10 billion yuan, when annual sales figures of two operators in China exceed 400 million yuan; or
- if the annual Chinese sales figure for the concentration is more than 2 billion yuan, when annual sales figures of two operators in China exceed 400 million yuan.

There are a number of relevant standards to be examined, such as:

- the market share and the relative power of control by the operators in such an environment;
- the level of concentration of the market;
- the level of influence of the operator on the entry by others into the market and on technological development;
- the level of influence of the operator on customers and other competitors; and
- the level of influence of the operator on national economic development.

The above is not an exhaustive list.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

The Anti-Unfair Competition Law of the PRC and the Anti-Monopoly Law of the PRC are the primary relevant legislation in this respect. Apart from the points discussed in other questions, under the Anti-Monopoly Law, a supplier abusing its dominant position in the market and requiring its distributors to purchase products from the suppliers designated by it for the purpose of excluding fair competition is prohibited.

The regulatory authority under the Anti-Unfair Competition Law is the administration for industry and commerce and the regulatory authority under the Anti-Monopoly Law is the Anti-Monopoly Commission. Both authorities have the necessary powers to investigate and impose administrative penalties.

Affected parties are entitled to bring actions under the Anti-Unfair Competition Law or the Anti-Monopoly Law for damages, loss of profits and reasonable investigation costs.

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

At present, Chinese law only allows parallel imports of patented products. The law does not specify whether parallel import of products under registered trademarks is prohibited, but there are cases where the parallel import of products under registered trademarks is regarded as an infringement of trademark rights. It is common to include contractual provisions to restrict parallel import, but instead of simply relying on the contractual arrangements, brand owners may record their registered trademarks with customs, and as a result, customs will monitor the shipments and seize any infringing products that bear the trademark. A registered patent is also recordable, but generally customs has difficulty in monitoring this due to lack of technical capability.

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

A supplier may advertise and market its products pursuant to the Advertisement Law of the PRC at its own cost, or pass all or part of its costs on to its distributors, or share in its costs upon mutual agreement.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

China is party to major international conventions on intellectual property protection. Following international practice, patents and trademarks should be registered in China in order to secure protection under local laws. Although a copyright work created overseas is automatically protected under local laws, in practice, a separate copyright record should be filed before the judicial and administrative authorities will recognise such rights. Trade secrets and confidential information are protected under the Anti-Unfair Competition Law of the PRC. Information that is not a trade secret or confidential relies heavily on the protection as stipulated in the relevant contractual documents between the parties. It is common for owners of intellectual property to enter into different kinds of agreements such as licensing and technology-transfer agreements with local parties.

It is prudent to conduct an audit to review the portfolio before entering into any negotiation with a local party, as there are usually some additional issues to be resolved (eg, Chinese transliteration of the brand should be registered).

26 What consumer protection laws are relevant to a supplier or distributor?

A distributor is not protected by the Consumer Interests Protection Law of the PRC, as, defined by this law, a distributor is not a consumer. However, under chapter 3 of the law, the supplier or distributor shall fulfil its statutory obligations as a business. For example, when selling its products to a consumer, the supplier or distributor cannot impose unfair or unreasonable transactional conditions on the consumer (eg, a tie-in sale). Apart from the Consumer Interests Protection Law of the PRC, the Tort Law and the Product Liability Law of the PRC set out the general obligations and liabilities of suppliers and distributors.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

China does not have a general law regulating product recalls, but there are several regulations concerning the product recall of specific categories of products, including automobiles, drugs, children's tools and foods. The requirements and procedures for product recalls are basically the same. Generally, manufacturers are responsible for product recalls and distributors or retailers are obliged to cooperate. A detailed action plan of the product recall must be filed with the authority.

Except in product recalls of automobiles where the relevant regulations stipulate that the manufacturer has to bear the cost thereof, other regulations are silent on which party is responsible for the cost. The parties in cases other than automobiles can negotiate the apportionment of liability and financial exposure in such product recall situations.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

Except for the mandatory warranties as set out in the Product Quality Law of the PRC, which covers the basic requirements on safety, use, and written descriptions and instructions of use, the supplier and distributors are free to negotiate additional warranties in their contractual arrangements, and to agree on the warranties to be offered to their downstream customers.

Update and trends

China's first E-commerce Law was adopted on 31 August 2018 and became effective on 1 January 2019. The E-commerce Law governs e-commerce platforms, individual merchants of these platforms and people who operate the business on their independent websites or other online service (eg, social networks). Under the E-commerce Law, an e-commerce operator shall register with competent authorities.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

Although the law is silent on the ownership of personal data of customers and end users, according to the Consumer Interests Protection Law of the PRC, business operators that collect the personal data of their consumers (including end users) are required to keep such information strictly confidential. Consent has to be obtained from the consumers before the exchange of personal data between a supplier and its distributor. The provisions on protecting the personal information of telecommunications and internet users, which is a general set of rules for the internet environment, further regulates the collection and use of personal data on the internet by dividing personal data into different categories. Different protection is offered for each category.

The first Cyber Security Law of the PRC was passed in 2016, and has been implemented from 1 June 2017. Under the Cyber Security Law, critical infrastructure providers (ie, companies running infrastructure critical to the economy such as public communications, energy, traffic, finance, etc) shall store all users' data on Chinese servers and undergo a security check if they want to transfer data out of the country.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

Chinese laws do not restrict these kinds of provisions, but it is advisable to have detailed provisions in this respect, as the court normally adopts a relatively restrictive interpretation for these types of clauses.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

In general, each business in China has to secure a business licence. From the administrative point of view, contracting with a business that has a business licence effectively designates a commercial relationship between two separate businesses. Furthermore, it is common to adopt provisions in the distribution agreement stating that the distributor is an independent contractor rather than employee of the supplier, and the distributor shall be responsible for its own actions.

In the event that the distributor or agent is an individual and a dispute arises on whether there has been an employment relationship, the PRC courts will consider the following aspects to determine whether there has been an employment relationship ('Notice on determining whether an employment relationship exists' Lao She Bu Fa [2005] No. 12):

- written agreement between the parties;
- whether the distributor is on the payroll and whether the supplier has paid any statutory social insurance for the distributor;
- whether the distributor has acquired any corporate identification, uniform from the supplier and made any authorised representation as the supplier's representative to the public; and
- whether the distributor completed any job application forms.

Having said that, practically, a properly set up distribution network should not give rise to such concern. As mentioned above, the existence of a business licence is the crucial factor in the determination in practice, as once such business relationship has been established, a distributor or agent with a business licence would not be deemed an employee of the supplier.

32 Is the payment of commission to a commercial agent regulated?

There are no specific laws or regulations governing payment of commission to a commercial agent. The general contractual law principles apply.

33 What good faith and fair dealing requirements apply to distribution relationships?

There are no good faith and fair dealing requirements applicable to distribution relationships in Chinese law. There is a 'fair and reasonable' principle under the Contract Law of the PRC, but this principle is not frequently applied. If applied, it is usually used to determine whether certain contractual provisions are oppressive instead of examining the course of dealing between the parties.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

There is no specific requirement governing distribution agreements to be registered with any government agencies. Instead, there are recordal requirements for intellectual property licence agreements. A trademark licence agreement should be recorded with the Trademark Office. Although such recordal is not mandatory, without it the licensing arrangement will not bind other third parties. A patent licence agreement should be recorded with the State Intellectual Property Office and is mandatory, otherwise the licensing arrangement will not bind other third parties. A copyright licence agreement should be recorded with the Copyright Protection Centre and is voluntary.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

The Criminal Law of the PRC provides two categories of corruptive practices offences. The first is against bribes offered to civil servants, and the other is against commercial bribery. There are different thresholds under the current prosecution policy, for example, in individual bribery situations, for bribes offered to non-public officials, the threshold of prosecution is 10,000 yuan. On the other hand, under the PRC Anti-unfair Competition Law (2017 Revision), as long as gifts or invitations may give the subject company or employees an advantage which is unfair to other competitors, any amount (whether provided in cash or in any other form) offered to non-public officials in exchange for business opportunities or interests will be subject to confiscation of illegal gains and a fine up to 3 million yuan, and if the circumstances are serious, the business licence of the subject company may be revoked.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

Apart from the issues covered above, the Contract Law of the PRC does not impose any specific restrictions or mandatory provisions on distribution contracts. The general contractual principles apply.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

Chinese laws do not impose any restrictions on the governing law of distribution contracts. However, in practice, if a local party files a lawsuit at the local court and the court proceeds with the case, it is unlikely that the local court will apply the governing law as set out in the distribution contract. Instead, the Chinese laws are likely to be applied.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

Chinese laws do not impose any restrictions as to the choice of courts or arbitration tribunals. However, since the performance of the distribution contract takes place within China, it is possible for the Chinese courts to assume jurisdiction over the case despite the choice of venue provisions.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

The procedures of the Chinese courts are relatively simple and normally a case can be closed within approximately a year. Under the present court rules, remedies are limited and certain relief such as injunctions and specific performance are not generally available.

Foreign parties' participation in Chinese court proceedings are common nowadays. Quality or predictable judgments can be seen in the courts of major coastal cities, although sometimes foreign parties may elect to have the disputes resolved in alternative venues such as arbitration in Hong Kong owing to the language barrier, and Hong Kong arbitral awards are enforceable in China. Under Chinese court and arbitration rules, there are no general disclosure obligations and evidence rules are less flexible (eg, electronic records and evidence should be notarised, evidence outside China should be legalised or authenticated by a Chinese Embassy or Consulate, and special attention should be paid at the preparation stage).

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

There is no formal mediation process under the rules, but judges and arbitrators usually suggest ad hoc mediation before the conclusion of the case.

Arbitration clauses are generally enforced, and the choices of the parties such as language, number of arbitrators and venue are generally respected. There are now several arbitration commissions within China, such as the China International Economic and Trade Arbitration Centre (CIETAC) in Beijing, the Shanghai International Arbitration Centre and the Shenzhen Court of International Arbitration. The second and third institutions were formerly sub-commissions of the CIETAC, in Shanghai and Shenzhen. Since both sub-commissions are now independent, an arbitration clause previously designating them as CIETAC sub-commissions should be revised, otherwise there may be an issue regarding the identity of the institution.

Arbitration is gaining popularity in cross-border commercial disputes because arbitrators are usually practitioners with substantial experience in the relevant areas and arbitration proceedings are more flexible in terms of the procedure.



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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

Yes. Whether from the European Economic Area (EEA) or not, inward investments are welcome. For private limited companies, generally, the only hurdle is the paid-in minimum share capital of €2,500. Depending on which by-laws (articles of association) you require, the cost of setting up a company varies between about €3,000 and €10,000, including the fixed registration fee, establishing a bank account and tax account for the purpose of income tax, VAT and the employer liabilities.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

There are no quota limitations for foreign participation.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

The private limited liability company is by far best suited. It can be formed by one person, whether physical or juridical. Mainly, all that is needed is to adopt the by-laws containing, at a minimum, the company name, domicile and field of operations, sign the memorandum of association that rarely fills more than one sheet of paper, and file the notification with the Companies' Registry: the Trade Registry, operated by the Finnish Patent and Registration Office. However, a person must be careful not to encroach upon anyone else's trade name or trademark, and be able to bring forth evidence to the effect that the subscribed number of shares has been fully paid for in advance to a bank account within the European Union, this being, additionally, confirmed by a chartered accountant and all the directors to be registered.

In principle, the Companies Act (624/2006), and for the incorporation procedure the Trade Registry Act (129/1979) and Ordinance (208/1979) govern them.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

In general, the foreigner-specific restrictions in respect of operating are limited to foreigners from outside the EEA and concern mainly the fields of defence, banking, financing and insurance. In general, there are no restrictions in respect of title to shares or business assets. However, a business operating in a narrow business sector, perceived as putting at risk an important national interest, such as in the business of banned dual-use goods requiring a licence for export, would be well advised, under the Monitoring Act (1612/1992), to seek formal permission from the Ministry of Employment and Economy. This notwithstanding, running a branch of a foreign entity from outside the EEA requires the consent of the Companies Registry. Normally, consent is readily granted. If the foreign business runs a Finnish subsidiary, at least one of the directors, including the managing director (eg, CEO, president), must be a resident of the EEA, unless the Companies Registry grants an exemption. The auditor should be a resident authorised or approved public accountant. In the event that there is no person within the EEA entitled to sign in the name of the subsidiary or the branch, there must be a registered agent for service of process in Finland.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

Yes. See question 4.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

According to the main rule, foreign businesses are taxed on income sourced in Finland only. On the formation of an importer owned by the foreign supplier, no tax is levied, just a modest handling fee.

Should the foreign business have a permanent establishment (PE) in Finland, it will be liable to tax on all income attributable to the PE. Moreover, dependent on its domicile and the kind and origin of the products imported, the foreign supplier may be subject to customs duties as well. In addition, with regard to its imports, the supplier may be subject to car purchase tax and excise duties levied on, for example, tobacco, alcoholic beverages, soft drinks and liquid fuels.

Given that foreign businesses are taxed only on income sourced in Finland, and that the foreign business will be liable to tax on all income attributable to the PE, sales revenue, interest, royalties and capital gains are included, but costs, expenses and losses attributable to the business are deductible. If a PE's business operation results in loss, such loss will be deductible during the subsequent 10 tax years, applying the same loss carry-forward rules that are applied in respect of Finnish business entities. However, these rules will not apply should more than half the ownership of the company change hands.

Dividends are generally totally tax-exempt both domestically and under either the EU Parent-Subsidiary Directive, subject to the 10 per cent minimum shareholding requirement, or tax-exempt to a quarter subject to a double tax treaty between Finland and the country from which the dividends are distributed. The corporate tax rate is 20 per cent. Since there are currently no thin capitalisation restrictions, a business can be financed from abroad, however, subject to some rather intricate rules on the deductibility of interests paid in excess of €500,000.

Generally, the tax treaties provide for tax on dividends and royalties varying between 5 and 15 per cent to be withheld at source. However, where the EU Parent-Subsidiary Directive is applicable, no withholding tax is levied on profit distribution, such as dividends, to a parent company holding, directly, at least 10 per cent of equity of the profit-distributing company. But where the Directive is not applicable, the withholding tax at source on dividends is 15 per cent.

However, for other non-resident corporate bodies, generally, the rate of withholding is 20 per cent on profit distribution, interest (where not completely tax-exempt) and royalties. For physical persons, the rate is 35 per cent on income from employment, pensions and distributions by employee investment funds, unless otherwise agreed in the tax treaty concluded with the recipient's country of residence. Most income of non-residents derived from Finland, other than above indicated, is taxed on an assessment basis.

From the viewpoint of the foreign business electing to use as its vehicle the limited liability company, it is notable that Finland has concluded 116 treaties for avoidance of double taxation and tax evasion, some of which are multilateral and take prevalence over domestic tax

law. The most frequent method for eliminating double taxation is the ordinary credit method.

Where there is no double tax treaty with the domicile state of the foreign taxpayer, the country's tax rights will be determined by domestic tax laws.

Non-Finnish residents are taxed in Finland on income sourced in the country, subject to any applicable treaties for avoidance of double taxation. Under certain conditions and subject to the approval of an application, salary earners with special expertise may, for a maximum period of four years, be entitled to participate in a regime permitting the employer to withhold, in lieu of income and municipality tax, 35 per cent of salary earned. Otherwise, alien employees will be liable for progressive tax on their salary or wages should they stay in Finland for longer than six months, regardless of citizenship. If the stay lasts no longer than six months, the Finnish employer will collect 35 per cent tax at source on the pay, as well as withhold social security payments unless the pay is effectuated by and encumbers a foreign company. Royalties paid to holders of intellectual property rights who are not Finnish residents are subject to a 28 per cent tax at source. The tax rate is 30 per cent for capital income, and 32 per cent where capital income exceeds €40,000.

In general, goods and services supplied in Finland in the course of business are subject to VAT. The general rate of VAT is currently 24 per cent, although the rate for food and restaurant and catering services is 14 per cent and the rate for categories such as books, subscribed newspapers, cultural events, medicines, fitness services, passenger transport and accommodation is 10 per cent.

Real estate tax is assessed on the taxable value of the property, whether land or buildings. Transfer of title to shares of a private limited liability company is generally subject to a transfer tax of 1.6 per cent of the price agreed. On transfer of real estate, the tax rate is 4 per cent.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

For both newcomers and established suppliers, the commercial agency provides a means of penetrating and exploiting the market as well as launching a selection of new products. For supply of heavy capital equipment, such as industrial machinery, the agent, whether the commercial or the undisclosed commission agent and with or without a consignment stock, comes in handy. However, frequently, best suited for products requiring local storage or modification is the variety of available open or closed distributorship arrangements, such as the dealer, the value-added reseller or the selective distributor, the latter mode being favoured by high-tech as well as luxury products manufacturers.

Apart from the business format franchise contract, the product distribution franchise contract is a recognised mode of distribution of, in particular, daily consumer products regardless of whether the following apply:

- the franchisee also carries products of suppliers other than those of the franchisor;
- the trademark is established;
- the system feature of the franchisor is weak or strong; or
- the services, such as training and continued assistance, are good or poor.

The same or similar applies to a variety of trademark licensing arrangements. An optional manufacturing licence contract may warrant the local distributor the ability to manufacture the quantities demanded should the supplier no longer be able to meet the demand. In particular, in the latter case, the manufacturer or supplier may wish to participate, by means of shareholding, in the business of its distributor.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

The fairly narrow concept of commercial agency is regulated by the Act on Commercial Representatives and Salesmen (417/1992) (the Commercial Agents Act). Such an agent, in the statute denoted as a commercial representative, is defined as an entrepreneur who, in a

representation contract concluded with another (the principal) has undertaken to promote, continuously, the sale or purchase of goods on behalf of the principal by obtaining offers for the principal or by concluding sales or purchase contracts in the name of the principal.

Thereby, outside the purview of the Act fall all other types of agents, such as the concealed agent and consignment or commission agent among others, as well as any kind of agency for the supply of services.

The relationship between a supplier and its distributors of goods or services is not regulated by any particular statute, but by a number of more or less general statutes, such as the Contracts Act (228/1929), the Sale of Goods Act (355/1987) and the Unfair Business Practices Act (1061/78). Of particular importance are the EU competition rules (see question 13).

The Competition and Consumer Authority (FCCA) is the government agency exerting certain power in respect of competition, but is generally regarded as lacking the means to effectively have an impact on consumer issues.

There is a host of self-regulatory constraints and guides that govern the distribution relationship, such as those published under the auspices of the International Criminal Court (ICC). One most prominent is the translation into Finnish of the Consolidated ICC Code of Advertising and Marketing Communication Practice 2011. In addition, there are a number of guidelines as to advertising and marketing. Moreover, there are the Council of Ethics in Advertising and the Board of Business Practice, both sub-agencies of the Finnish Central Chamber of Commerce and specialised in business-to-business sales and marketing issues. In particular, for convincing courts and arbitral tribunals on ethical advertising and fair business practice, the opinions of these two bodies are held in high esteem.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

No, freedom of contract prevails. Apart from where the contract is made for a certain duration, the prevailing opinion is that a party to a distribution relationship cannot be forced to be bound, perpetually, and accordingly, unless the parties contractually agree otherwise, both parties are deemed to be allowed to terminate the contract without any specific cause. The aforementioned notwithstanding, there ought to be a certain period of time within which the opposite party may adapt themselves smoothly to the change of circumstances, and therefore, the length of the period of notice may vary depending on a number of reasons.

Any clause to the effect that the contract term may be renewed provides for accommodating to the changed circumstances.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

Save where the relationship is qualified as that of commercial agency, there is no mandatory compensation or indemnification due to the distributor, commission agent or self-employed intermediary solely for the reason that the contract was terminated without cause. However, where essential properties of the relationship are similar to those of a commercial agent, case law suggests the courts may be inclined to make use, analogously, of the provisions of the Commercial Agents Act harmonised to article 17, paragraph 2 of the EU Directive 86/653/EEC (Council Directive of 18 December 1986 on the coordination of the Member States relating to self-employed commercial agents). (Implications of such analogous application can be found in Supreme Court case KKO 42 (1987).) Where the relationship is terminated without taking heed of the need for providing for a period of notice enabling the opposite party to accommodate him- or herself to the changed circumstances, the intermediary should be able to count on being compensated for the loss caused. Of course, the same is true where the termination can be demonstrated as being abusive.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

Based on the principle of freedom of contract, yes. However, the general rule of the Contracts Act admitting the competent court to adjust a contract provision found unconscionable has been applied in court practice on a number of occasions. The main thrust of the rule is that should the court deem a contract term unfair or the application of such term leading to an unfair result, the term may be adjusted or set aside (section 36 of the Contracts Act as amended by Law 956/1982). In particular, should the distributor or agent run the risk of going out of business because of a contract provision prohibiting him or her at the peril of payment of damages from transferring the ownership of his or her business, for a lengthier period of time and with no regard to the change of circumstances, the court may determine such provision be considered grossly unfair, unreasonable or otherwise unconscionable.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

No, there are none. But in respect of confidentiality provisions, the general rule of the Contracts Act admitting the competent court to adjust a contract provision found unconscionable may be applied.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

Restrictions are generally enforceable subject to being in compliance with the applicable competition laws, which according to the main rule provide that a competition prohibition as to competing goods or services must not, during the contract term, last for longer than five years or for one year after termination, except where by derogation permitted pursuant to the applicable competition rules (Commission Regulation (EU) No. 330/2010, article 5, paragraphs 2 and 3, on the application of article 101(3) of the Treaty on the Functioning of the European Union (TFEU) to categories of vertical agreements and concerted practices). It has to be remembered, however, that the above notwithstanding, the members of a selective distribution system must not be, whether directly or indirectly, imposed any obligation causing such members not to sell any brands of competing suppliers.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

No, the supplier is not even permitted to set maximum prices not to be exceeded by the distributor since such practice interferes with the distributor's freedom to set his or her own prices. However, by means of price recommendations the supplier may influence resale pricing provided those recommendations do not amount to resale price maintenance or price fixing, which is strictly prohibited under domestic and EU law, whether directly or indirectly, such as by means of determining the distributor's sales margin or maximum reductions to be granted to customers.

Resale price maintenance in vertical agreements is a hardcore restriction considered by the antitrust authorities as unlawful and not exemptable. Since, in most cases, the commercial agent is integrated in the principal's sales network and also otherwise a genuine agent, the agent remains outside the scope of the competition rules concerning price maintenance.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

Resale price recommendations and suggestions are permitted, but establishing a minimum advertised price policy may, depending on its contents, be branded as anticompetitive. This, however, would not foreclose advertising recommended prices. Nevertheless, any

defensive boycott in order to punish violations of agreements that restrain competition are prohibited types of discrimination. The same is true of any predatory boycotts.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

There are no restrictions on including a most-favoured-customer clause in the contract.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

There should be no obstacle to applying different prices to different types of customers, in different locations, granting different rates of discount to individual customers and so on, provided the criteria are not arbitrary and are applied consistently.

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

The supplier may make the distributor refrain from actively selling to certain geographical areas or categories of customers, but not from selling passively, and only if these geographical areas or categories of customers are exclusively reserved for the distributor, agent or the principal him- or herself. However, in the event of a selective distribution system, the rule expressly authorising the restriction of sales by the members of a selective distribution system to unauthorised distributors within the territory reserved by the supplier to operate that system is applicable (Commission Regulation (EU) No. 330/2010, article 4b, section iii on the application of article 101(3) TFEU to categories of vertical agreements and concerted practices).

Exclusive territories are permitted, in principle, and are customary. A supplier may reserve certain customers to itself, as discussed above.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

The general rule is that a supplier may not restrict or prohibit e-commerce sales by its distribution partners. However, the supplier may require certain qualitative criteria of the e-commerce. Neither can the supplier restrict or prohibit passive reselling outside the distribution partner's assigned territory. However, restriction of active sales outside a distributor's assigned territory is permitted.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

Unless refusal to deal amounts to abuse of a dominant position or is deemed to be unfair business practice, such refusal is part of the freedom of contract.

Apart from making the distributor refrain from active sales in certain geographical areas or to certain categories of customer, within the frame of a selective distribution system the supplier may restrict its distributor's ability to deal with unauthorised distributors outside the territory of the system (ie, non-members of the system).

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

At least in principle, under the merger control rules, a distribution contract may be deemed a reportable transaction if the supplier exploits market power in trading relationships with distributors to earn excessive profits or gain other advantages. The contract can also require clearance if it amounts to the supplier exerting exclusionary or predatory abuses, such as the imposition of unfair selling prices or conditions not falling within the sphere of the vertical restraints generally applied

to distribution contracts. Such practices eventually result in concentrations increasingly deteriorating the conditions for competition which may be fateful in a small market, such as the Finnish market. Under the merger control rules, a distribution contract is a reportable transaction requiring clearance by the competition authorities where the combined turnover of the parties exceeds €350 million and the Finnish turnover of at least two of the parties exceeds €20 million each.

The standard used for evaluating the transaction, as to the calculation of the turnover, is the government decree on the calculation of turnover of parties to the concentration (1011/2011), and the standards and practices described in the Guidelines on Merger Control issued by the FCCA. If the concentration falls within the scope of Council Regulation (EEC) No. 139/2004 on the control of concentrations between undertakings, the acquisition shall be notified to the European Commission, which has the sole right to examine the concentrations having a Community dimension.

Unless it is about an untrue or non-genuine agency agreement, the agent as an auxiliary of his or her principal remains beyond the anti-trust rules.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

Although single branding is frequently implemented by means of a non-competition clause, it can also occur otherwise and be objectionable without either a five-year or one-year period of grace (see question 13). This is the case if competitors are excluded from the market. Tying arrangements may affect both the markets for those manufacturing the relevant products as well as the price of the products. In addition to the prohibitions against anticompetitive agreements, there is the prohibition against abuse of dominance that constrains the relationship between suppliers and their distribution partners.

Suppliers and their distribution partners must comply with section 5 of the Competition Act (948/2011) and articles 101 and 102 TFEU. The competent agency to enforce such laws is the FCCA.

Private parties can bring actions under antitrust or competition laws. Liability in damages under section 20 of the Competition Act is due to anyone who has suffered damage or loss because of infringement of sections 5 or 7 of the Competition Act, or articles 101 or 102 TFEU.

The available remedies are damages for economic loss, whether direct or indirect, including but not limited to expenses, price difference and lost profit. Any losses because of price discrimination, excessive pricing due to a cartel or the refusal by a party in a dominant position to supply are deemed as direct losses to be compensated.

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

No, save for selective distribution (Commission Regulation (EU) No. 330/2010, article 1(e) on the application of article 101(3) TFEU to categories of vertical agreements and concerted practices).

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

The main provisions are contained in the Unfair Business Practice Act requiring truthfulness in connection with all sales and marketing, including advertising, and in the Consumer Protection Act (38/1978) regulating sale and marketing to consumers.

There is no statutory limit with regard to whether a supplier may pass all or part of its cost of advertising onto its distribution partners or share in its cost of advertising.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

Safeguarding of intellectual property rights (IPRs) is implemented mainly contractually and by means of registration. Any one individual

having made an invention susceptible to industrial application, or his or her successor in title, is entitled, on application, to a patent. Exclusive rights for a trademark may be acquired, even without registration, after the mark has become established. A trade symbol is considered established if it has become generally known in the appropriate business or consumer circles in Finland as a symbol specific to the goods or services of its proprietor. Any artistic or literary work, independently originated by a human being, and of original character, expressed in any manner or form, qualifies for copyright. In respect of software and databases, sheer originality is enough. The requirement fulfilled, copyright arises by virtue of itself. Only copyright, know-how and trade secrets can be registered.

The supplier is encouraged to safeguard its IPRs by means of provisions to the effect that the distributor is under a duty to inform the supplier of infringement of its IPRs, to assist it in defence of its rights and not to reveal, either during the currency of the contract or after its termination or expiry, the supplier's trade or commercial secrets or other confidential information, such as know-how and technical data, nor to use such secrets or confidential information for purposes other than those of the contract.

Technology-transfer agreements are common.

26 What consumer protection laws are relevant to a supplier or distributor?

A number of laws and decrees supplement the Consumer Protection Act (38/1978), such as the Act on Provision of Information Society Services (458/2002) and the Communications Market Act (393/2003), both aiming to ensure reasonably priced communication services for consumers. In addition, there is the Consumer Safety Act (920/2011), the Act on the Safety of Toys (1154/2011) and the ancillary government decree, plus the decree on certain chemical requirements concerning toys (1352/2013). Moreover, there are the Government Decrees on the Data to be provided on Consumer Goods and Services (613/2004), on Price Information on Consumer Products and Services (553/2013), and concerning unfair business-to-consumer commercial practices (601/2008, implementing the EU Unfair Commercial Practices Directive 2005/29/EC); the Food Act (23/2006); the Accommodation and Nutrition Agency Act (308/2006); the Package Tour Agency Act (939/2008); the Act on the Provision of Services (implementing Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market, 1166/2009); the Insurance Contracts Act (543/1994); the Debt Collection Licence Act (517/1999) as well as a host of provisions concerning investment guidance. Generally applicable supplemental statutes are the Interest Act (633/1982), the Debt Collection Act (513/1999) and the Criminal Code (1889/39), the latter of which includes chapters on business offences and on offences endangering health and safety (consumer credit offence (Criminal Code, Chapter 30, section 3), charter trip company violation and charter trip company offence (Criminal Code, chapter 30, section 3a), health offence (Criminal Code, Chapter 44, section 1)).

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

Any consumer product found perilous to a person's health or property where the peril is unavoidable by any other means can, by the local regional state administrative agency being supervised by the Safety and Chemicals Agency, or by the Safety and Chemicals Agency itself, be ordered, inter alia, to be recalled at the expense of the distributor. The same applies to consumer products lacking the CE marking denoting conformity with the relevant EU requirements (Consumer Safety Act (920/2011), Chapter 6).

Freedom of contract provides that there are no restrictions on the agreement delineating which party shall be responsible for carrying out and absorbing the cost of a recall.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

As a general rule, the principles of freedom of contract provide that there is no obstacle to such agreement between parties, albeit not in

relation to any third party. In addition, parties must take heed of the provisions permitting courts, at the request of the opposite party, to 'rewrite' the contract. See question 11.

However, the Consumer Protection Act period of six months' defect assumption from passing of the risk to the consumer cannot be validly limited to the disadvantage of a consumer. In terms of Finnish consumer law, a warranty always refers to the assumption of liability by the seller for the fitness or other characteristics of the goods or services, for a fixed period of time, and is, accordingly, to qualify as an advantage to the consumer. Any goods or services, whether consumer or not, must always meet the specifications set out in any guarantee statement or relevant advertising under pain of the consumer being eligible to claim cancellation of the purchase or alternatively price reduction, and in either case compensation for their loss.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

Yes. The Personal Data Protection Act puts the Finnish distributor under a number of obligations to ensure that all personal data is processed in accordance with the standards and requirements specified therein. For the purpose of the Personal Data Act personal data means any information on a private individual and any information on his or her personal characteristics or personal circumstances, where these are identifiable as concerning him or her or the members of his or her family or household, and processing means collection, recording, organising, use, transfer, disclosure, storage, manipulation, combination, protection, deletion or erasure of personal data, as well as other measures directed at personal data (Personal Data Act (523/1999), sections 3 and 8). On transfer of personal data to a third country, the Personal Data Act states that a transfer may take place only if that third country ensures an adequate level of protection, or if the European Commission pursuant to its competence under the Data Protection Directive finds that a third country ensures an adequate level of protection by reason of its domestic law or its international commitments. In addition, the statute states, expressly, that insofar as the Commission has declared that some a third country does not afford an adequate level of protection of personal data, transfer of personal data is not permitted to such country. Thus, Finland is to comply with the *Maximilian Schrems* decision of 6 October 2015. However, there are a host of exemptions providing for subterfuges. Such is the dubious permitting transfer of data 'for the conclusion or enforcement of a contract', considered to the benefit of the data subject, between the processor or controller and a recipient or third party.

The title to data protected under the Personal Data Protection Act is not regulated statutorily. Therefore it must be deemed as being the property of the one who has collected it, their successor or assignee.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

Such contractual provision is, in principle, enforceable. Apart from the risk of illegitimate use of such provision, it may, however, in practice, ensue in making the distributor the subordinate of the supplier to such a degree that he or she may be regarded as being an employee of the supplier.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

To be considered an employee, and be at least in part submitted to labour law, the distributor or agent is to be considered as acting under the direction and supervision of the supplier and, simultaneously, lacking the responsibility for financial risk. Small income may alone constitute a factor putting the distributor or agent in a position equal to that of an employee. It may appear that the distributor or agent is submitted to work under the direction of the supplier where involvement, in person, is required, or where the supplier is entitled, at its discretion or very frequently, to issue new instructions to the distributor or agent, the latter being required to adhere to such instructions and

the supplier allowed to monitor this adherence, or where the supplier is permitted to amend the contract at its discretion. Accordingly, importance is placed on the consciousness and intent of the parties as well.

If the distributor or agent is found to be a de facto employee and not an entrepreneur, the result may be claims against the supplier for vacation benefits and for such protection against dismissal, termination or whatever severance that an employee is considered to deserve under the Employment Contracts Act (55/2001) and, for social security purposes, claims from authorities considering the supplier liable for undeclared social security premiums. Although of course rather rare, such qualification as an employee for the purpose of the benefits extended under labour law may become constituted because of careless or negligent contract drafting, or because the arrangement in reality is allowed to degenerate into a state in which the distributor or agent is acting under the supplier's direction and supervision and not as an independent entrepreneur putting capital at risk. This may be the case where supplier-owned outlets are converted into franchises. One method of diminishing the risk of confusion that is advocated by some experts may be to see to it that the distributor or agent is a limited liability company instead of a sole proprietor.

Should the above criteria for the distributor or agent to be considered an employee exist, and should the distributor or agent, simultaneously, have failed to take out and maintain an insurance policy for at least the minimum statutory pension scheme in his or her trade, for the purpose of pension insurance premiums, he or she may be regarded as an employee, and consequently, the supplier may become liable for such insurance premiums, including any in arrears as well as default interest.

Again, in the event that the above criteria for a distributor or agent to be considered an employee exist, and the distributor or agent fails to pay the advance taxes or the final taxes assessed, the risk exists that the tax authorities will consider the distributor or agent an employee, and accordingly debit the taxes in arrears with the latter. Under these circumstances, also the question of the supplier's vicarious liability arises whereby the supplier may be held liable for the acts of the distributor or agent.

Whenever there is doubt as to whether the distributor or agent is to be regarded as an independent entrepreneur, it is advisable to seek a ruling from the tax authorities.

A supplier can protect itself against responsibility for potential violations of labour and employment laws by its distribution partners by means of not depriving the self-employed intermediary of its independence, as discussed above and by means of contractual stipulations to the effect that the distribution partners indemnify and hold the supplier not liable for any consequences of being deemed an employee, such as making good any amounts it may have to pay to such employee as well as to any third parties for the benefit of the employee of the distributor.

32 Is the payment of commission to a commercial agent regulated?

The payment of commission is provided for under the Commercial Agents Act (Act on Commercial Representatives and Salesmen, sections 10 to 15). In the event that the parties have failed to agree on the payment of commission, the commercial agent is still entitled to commission on any transaction concluded during the period of validity of the agency contract where the transaction has been concluded as a result of his or her action or with a third party whom the agent has previously acquired as a client for the principal for transactions of the same kind or, if the agent has been entrusted with a specific geographical area or group of clients, the transaction has been concluded with a third party belonging to that area or group of clients.

Moreover, the agent is entitled to commission on any transaction concluded after the termination of the agency contract if the transaction has been concluded in the manner referred to above and the offer, whether to purchase or to sell, reached the principal or the agent prior to the termination of the agency contract or if the transaction can be deemed mainly attributable to the contribution of the agent during the period of validity of the agency contract and the transaction was concluded within a reasonable period after the termination of the contract. Any contracting to the effect that the right to commission is to arise later than at the time when the third party has fulfilled his or her performance obligation, or should have done so if the principal had fulfilled

his or her performance obligation in accordance with the transaction, does not bind the agent.

Unless the agent consents thereto, the agent's right to commission is not affected should the principal agree with the third party on cancelling the transaction or amending its terms. In the absence of any agreement on the amount of the commission payable, the commission shall be determined on the basis of the remuneration customarily paid for the execution of the same or corresponding activities at the location of the agent's operating. If, therefore, the amount of the commission cannot be determined, the agent is entitled to a commission that is reasonable under the circumstances. The payment shall be effected by the end of the calendar month during which the commission accrued.

33 What good faith and fair dealing requirements apply to distribution relationships?

The requirement that the contract must be negotiated and executed in good faith is emphasised in Finnish jurisprudence. The concept of good faith also underlies the Contracts Act, which is the basis of each and every distributorship founded on Finnish law. Accordingly, the principle of *culpa in contrahendo* is also emphasised. The carrying force is loyalty between the parties and each party ought to deal loyally, also paying attention to the advantage of the other party. Therefore, when interpreting a contract, weight is primarily given to the following issues:

- in a like situation, how do parties normally act;
- what is to be assumed from the parties;
- what prudence and due diligence require in any particular trade;
- what purposes does the contract serve;
- what ends did the parties have in mind (any disloyal intentions); and
- at what stage did the parties know what?

For commercial transactions between the supplier and the distributor, the Sale of Goods Act is founded on the concept of good faith as well as fair dealing. The same is true as to the Contracts for the International Sale of Goods, which is the assumed applicable set of rules for the sale of goods in trade outside of the purview of the Nordic countries. Insofar as the element of representation is concerned, the analogous application of the Commercial Agents Act requires that regard be paid to the duty of both the agent and the principal, among others, to act in good faith towards one another (Act on Commercial Representatives and Salesmen, sections 5, 8 and 9).

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

No. There is no requirement that the agreements as such should be registered with or approved by any authorities to be deemed valid or for whatever purpose. However, where either party to a licence of an IPR desires that the licence be recorded by the relevant registry, such non-mandatory recording is possible. Recording makes the licence effective against third parties, such as creditors.

In addition, a security interest by means of a pledge can generally be instituted by the recorded owner of the IPR. This is true for registered trademarks as well as patents, utility models, registered designs, layout designs and plant varieties. However, unregistered trademarks, trade names and copyrights cannot be used as security. A valid pledge of a right to a registered trademark requires a writ of pledge and entry into the register of trademarks. Execution can be levied on a trademark only if the pledge is entered into the register. Although as to the pledge of a patent right, there are no formal requirements inter partes for being regarded as binding in relation to third parties, the pledge needs to be entered into the register of patents. In these respects, one should note that there are some slight differences compared with other pledgeable IPRs.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

The anti-bribery and anti-corruption laws, from the most simple to the more refined, are, indeed, applicable to suppliers and their distribution partners. Pursuant to Chapter 30 of the 1889 Penal Code, there is a wide range of acts containing taking or offering of bribes being encompassed by the punishable offence of bribery in business. Moreover,

Update and trends

Where Finnish law is applied or Finnish jurisdiction concerned, the Supreme Court's 3 May 2018 judgment in the *Meira* case (KKO 2018:37; dissent 3 - 2) establishes a caveat for any distributor, whether domestic or foreign, where Finnish law is applied or jurisdiction is concerned. In a nutshell, the outcome of the case was that the supplier of certain products furnished with the brands of the buyer and who, therefore, was unable to dispense of his stock prior to the expiration of the contract, was awarded no damages or compensation. What is baffling is that the Court recognised that European Private Law (Principles, definitions and Model Rules of European Private Law, DCFR) prompts the party whose products have been brought onto the market to repurchase, at a reasonable price, the remaining stock held by the party who may be unable to resell such stock so as to avoid the latter suffering unreasonable losses because of termination of contract, but it still decided to the contrary. Since the same may well be applied to any distributor who has purchased in advance a stock it may be unable to get rid of during the brief period of termination either agreed or granted by case law, there is a factual risk any distributor whose case is entertained by a Finnish court or arbitral tribunal, or under Finnish law may face a similar treatment as the supplier in the *Meira* case.

there is a host of other wrongful acts and corruptive behaviour that are punishable and applicable to all conceivable arrangements concerning distribution of goods or services.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

No, there are no other restrictions on provisions in distribution contracts or limitations on their enforceability. There are no mandatory provisions, save for the above-mentioned good faith, fair dealing and loyalty between the parties.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

No. Under article 3 of the Rome I Regulation (EC) 593/2008, the parties to the contract may subject a distribution contract to the law of a foreign country, or may elect a foreign law to be applicable to a certain separable part of the contract. Nevertheless, regarding choice of a foreign law, whether accompanied by the choice of a foreign tribunal or not, such choice must not prejudice the application of domestic mandatory rules from which no derogation can be made, such as the rules of the law on consumer protection, product liability, labour and employment, personal data law, law of tenancy, law on restraints of competition, procedural rules as to IPRs or tax law.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

Yes, there are restrictions, although they do not seem to affect agency or distributorship contracts. The restrictions seem to be limited to matters outside the scope of EC Regulation 2015/2012 and the rules conferring special jurisdiction to consumers under section 4 of the regulation as well as exclusive jurisdiction in certain matters under section 6 of the same regulation. Since prorogation of jurisdiction is provided for under article 25 of Regulation 2015/2012 to the effect that if the parties, regardless of their domicile, have agreed in the form prescribed that a court or the courts of a member state are to have jurisdiction to settle any disputes that have arisen or that may arise in connection with a particular legal relationship, that court or those courts shall have jurisdiction, unless the agreement is null and void as to its substantive validity under the law of that member state. Such jurisdiction shall be exclusive unless the parties have agreed otherwise.

Similarly as a prorogation agreement is recognised, so is the purported derogation agreement, which is an agreement to the effect that a certain court is (or certain courts are) to be regarded as foreclosed (ie, excluded) jurisdiction.

Parties can contractually agree to arbitration of their disputes instead of resorting to the courts. Arbitrations can be seated abroad provided that the seat of the arbitration is a signatory to the New York Convention.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

The courts available to suppliers and distribution partners to resolve their disputes on contract performance and commercial transactions are in the first instance the ordinary district courts. In civil cases the proceedings start with the pretrial phase of the procedure, after which the case is adjourned to the main hearing. Alternatively, the case may be resolved already in the course of the partly written and partly oral pretrial procedure. Apart from the claims and merits of the case, the complexity and length of the procedure depend to a great deal on, first, the quality and quantity of evidence to be presented and, second, the fact that each party is heard regarding the claim, its grounds and whatever evidence there is.

Should the judgment or decision rendered, within about a year or two, be contrary to expectations, non-satisfaction and the intention to appeal is to be notified within a week and generally the appeal is to be accomplished within 30 days. The appeal procedure consists of written preparation and one or more hearings. The courts of appeal have to arrange an oral hearing if the evidence of the case has to be evaluated once more, or when a party so requests unless the appeal is, for example, clearly without merit.

The third and final instance is the Supreme Court, which has its seat in Helsinki. Its main task is to establish precedents, thus giving guidelines to the lower courts on the application of the law. The Supreme Court may grant a leave to appeal in cases in which a precedent is necessary for the correct application of the law, a serious error has been committed in the proceedings before a lower court or another special reason exists in law. Normally, the cases are decided on the basis of solely written material. The Supreme Court may, however, also conduct oral hearings and inspections.

Finally, the Market Court is the competent court as regards disputes on, inter alia, competition between firms and improper marketing. Redress is sought with the Supreme Court.

Foreign businesses are encouraged to use the local courts. A standing joke goes that foreign businesses can expect equally unfair treatment as anyone else.

The statute says that anyone who wishes to present evidence in advance for a case that is not yet pending shall apply for permission for this from a court of first instance. If his or her rights depend on the admission of the evidence and there is a danger that the evidence will be lost or that it will be difficult to present it later, and the presentation

of the evidence is not for the purpose of obtaining information on an offence, permission shall be granted. If the rights of another person depend on the presentation of the evidence, he or she may, if necessary, be invited to appear in court for the hearing. His or her costs shall be covered by the applicant. In such cases no one may be required to appear as a witness or an expert witness in a court other than the court of first instance in the district of which he or she resides or is staying (Code of Judicial Procedure (AAD/1734), Chapter 17, section 10).

Once the case is pending, pretrial disclosure of documents (discovery) is implemented by the request of either party that the opposite party states whether he or she has in his or her possession written evidence or an object that may be relevant in the case, always provided such document or object be sufficiently identified by the requesting party (Code of Judicial Procedure (AAD/1734), Chapter 5, section 20, paragraph 2). When it can be assumed that a document is of significance as evidence in a case, the person in possession of the document can be ordered on pain of a fine to present it in court (Code of Judicial Procedure (AAD/1734), Chapter 17, sections 10 to 17).

One advantage of a foreign business resolving a dispute in the Finnish courts is the direct enforceability against a Finland-domiciled party, or one with property in this country. Another is that the court fees and dispatch costs are fairly low. In addition, as Swedish is formally a domestic language equal to Finnish, one more advantage is that should you wish to have your case tried completely in Swedish, you are entitled to expect your case to be equally thoroughly tried as if it were in the Finnish language. Certain matters, such as applications for injunctive relief, are often rendered timely, and effectively handled by able judges and service-minded court clerks. However, a serious drawback is the fact that since there is no statutory ceiling in respect of the prevailing party's attorneys' fees to be compensated by the defeated party, the risk of litigation tends to increase rapidly and uncontrollably.

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

Yes, such an agreement is enforceable, although whatever decisions mediation may bring forth are, in contrast to arbitral awards rendered in a New York Convention country, not enforceable. The award, however, needs to be recognised. This is dependent on whether the arbitration agreement on which the award has been founded fulfils the formal requirements and it must not be contrary to Finnish public policy. The party against whom enforcement of an arbitral award is sought shall, in general, be heard. Accordingly, should the party against whom enforcement is sought be able to demonstrate that one or more of the aforementioned obstacles exists, the award is not to be enforced.

An arbitration agreement concluded under Finnish law needs to be made in writing. This requirement is fulfilled if the agreement

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is contained in a document signed by the parties or in an exchange of letters between the parties. The written form requirement is also regarded as fulfilled where the parties, by exchanging emails, have agreed that a dispute shall be decided by one or more arbitrators. Any stipulations concerning the arbitration tribunal, the location of the arbitration or the language of the arbitration are matters that may affect the assessment to be conducted whether the rule of the Contracts Act admitting the competent dispute resolving body, be it a court or an arbitration tribunal, to adjust a contract provision found unconscionable should be applicable. See question 11.

The main advantages for a foreign business resolving a dispute with a business partner by arbitration in Finland are avoiding the quagmire of what, at worst, may evolve from any ordinary court, the fact the hearings are not public, the finality of the award and, lastly, the frequent ambitiousness and dedication of the arbitrator resulting in elaborated and well-founded awards, which in turn lead to continued demand for the fairly well-paid assignment of acting as arbitrator. The disadvantages are the expenses for both counsel, compensating the arbitrator or arbitrators for their work and expenses and, for the defeated party, the lack of any way of seeking redress.

Germany

Martin Rothermel and Benedikt Rohrßen

Taylor Wessing

Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

Yes. Specific restrictions may apply, however, if (foreign or domestic) investors do business in the defence, pharmaceutical or financial sectors.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Yes. There is no specific investment legislation and no minimum percentage of German shareholders required.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

The types of business entities suited best are:

- limited liability company (GmbH and UG);
- stock corporation (AG); and
- limited partnership (KG).

The criteria for choice of entity used are liability, taxation, financing, personal involvement and control, and flexibility. For larger companies, GmbH or AG are typically best suited. Their shareholders' liability is limited to the respective share capital.

The minimum share capital varies between €50,000 (AG), €25,000 (GmbH) and €1 (for the GmbH-subtype, UG). The transfer of shares in a GmbH or UG typically has to be approved by the other shareholders and notarised, while shares in an AG are freely transferable. However, the GmbH is a more flexible and procedurally less demanding form of entity than the AG.

GmbH, UG and AG entities are formed by one or more founding shareholders, adopting the articles of association and appointing their managing directors plus, in the case of an AG, a supervisory board (of at least three members) in a notarial deed. They exist upon registration at the commercial register. Alternatively, a supplier may purchase an existing, inactive shelf company and, as an advantage, start operating immediately.

Partnerships are often preferred for tax reasons, especially the KG, which – for reasons of limiting liability – is often combined with a corporation as general partner (GmbH & Co KG or AG & Co KG). They require at least two partners.

The governing laws are as follows:

- the Limited Liability Companies Act for the GmbH and UG;
- the Stock Corporation Act for the AG; and
- the German Civil Code (BGB) and the German Commercial Code (HGB) for partnerships.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

Generally, no: foreign businesses operate under the same rules as domestic businesses. By way of exception, the Federal Ministry for Economy and Technology can restrict or prohibit acquisitions of or participations in domestic business entities by individuals or business

entities seated outside the European Union, Iceland, Liechtenstein, Norway (together, the EEA) or Switzerland. Preconditions to this are:

- the foreign investor acquires 25 per cent or more of voting rights in a German company; or
- the acquisition endangers national public order or security (sections 55 to 59 of the Foreign Trade and Payments Ordinance). This may especially be the case if the domestic business entity acquired pertains to infrastructure sectors (telecommunications, power supply, trains, airports or hospitals).

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

Yes. See question 4.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

A foreign supplier especially has to consider:

- whether the importer itself shall pay income tax, or the supplier as owner, or both; and
- whether the supplier might be subject to double taxation (both in Germany and its state of origin) and whether it can be avoided.

To foreign businesses and individuals that operate in Germany, two levels of taxation apply:

- the trade tax applies to all businesses and individuals in Germany and is paid on taxable earnings. As a local tax, its rate differs from municipality to municipality; and
- the income tax depends on the business entity.

Corporations are subject to corporate income tax (15 per cent flat rate) and their shareholders to a tax on capital gain and dividends. The average overall tax burden for corporations in Germany is 30 per cent (corporate income tax and trade tax).

A partnership itself is not subject to income tax, but its partners are, to either corporate (if business entities) or personal (if individuals) income tax.

Individuals pay personal income tax. The tax rate increases with the income (to a maximum of 45 per cent at an income of €250,000), but trade tax payments can be set off against it. Special tax rates apply for dividends and capital gains.

For dividends, capital gains, interest payments and licence fees, withholding tax may apply. It amounts to 25 per cent of the capital gain distributed to the owning business (plus a further 'solidarity surcharge' of 5.5 per cent, added to the tax amount). These taxes may be refunded in case of double taxation if a respective treaty with the country of origin of the owning business exists.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

Any conceivable distribution structure is available. Apart from manufacturing under a private label, trademark licensing and joint ventures, the following distribution structures are typically used:

- In-house sales force, allowing direct influence on employees and an easy margin calculation, but generally entails high labour cost (including social security).
- Self-employed commercial agents, who solicit customers and can (but do not have to) have the authority to conclude a contract on the supplier's behalf. The supplier sells directly to the customers and bears the distribution risk, but may also control the margins. Contrary to employees, the agent's remuneration (commission) can be exclusively profit-oriented (ie, remunerated only in case of successfully soliciting customers), and in relation to the turnover. Commercial agents have to provide detailed market reports. If the commercial agent acts in the European Union, protective agency law applies, including the indemnity claim (see questions 8 to 10).
- Distributors, who buy and sell the products on their own behalf. Consequently, they bear distribution risks, and, in return, gain profit from the difference between purchase and resale price, while suppliers' margins are rather low. The distributor is obliged to market and distribute the supplier's products, and to safeguard the supplier's interests. Distributors are less protected than commercial agents (for exceptions, see question 8).
- Commission agents, who are midway between commercial agents and distributors. They sell products in their own name but for the supplier's account. The supplier bears the sales risk, even if the commission agents have products in a consignment stock to which the supplier retains the title. The supplier can influence the commission agent without observing the strict antitrust law that applies to distributorship agreements.
- Franchisees, who buy and sell products on their own behalf. The franchisee acquires licences of intellectual property rights (trade-marks and know-how) from the supplier (franchisor) for using and distributing the products or services. The franchisee is entitled and obliged to design its shop according to the franchisor's concept and corporate design, and use the management- and system-specific know-how. In return, the franchisee pays royalties. The franchisor has, in the beginning, to disclose the key risks and issues for running the franchise, and subsequently often provides assistance on know-how and business.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

Employment contracts

Employment contracts with the in-house sales force are governed by sections 611 to 630 BGB and several laws on employees' protection.

Agency contracts

Agency contracts are governed by sections 84 to 92c HGB. The commercial agent is, like the employee, strongly protected, for example, by mandatory rules on:

- minimum notice periods (see question 9);
- commission payments (see question 32); and
- goodwill indemnity (see question 10).

Distributorship contracts

Distributorship contracts are – as in most EU member states – not explicitly governed by statutory law. However, there is extensive case law, for example, on whether the supplier has to take back unsold products upon termination of the contract. Agency law applies by analogy if the distributor is:

- integrated into the supplier's sales organisation; and
- obliged (due to agreement or factually) to forward customer data during or upon termination of the contract.

Further, distributorship contracts have to conform to antitrust law. Generally, the antitrust law of any affected market applies (article 6(3a) of the Rome II Regulation).

Franchise contracts

Franchise contracts are not explicitly governed by statutory law. They combine elements of licensing, sales and management of another's

affairs. Generally, agency law applies by analogy (see German Federal Court of Justice (BGH), decision of 17 July 2002).

Certain industry self-regulatory constraints exist, for example, in the automotive industry, where members of the European Automobile Manufacturers Association have agreed to a code of good practice.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

The supplier's right to terminate without cause is restricted. No restriction applies to a decision not to renew the distribution relationship when the contract term expires, unless antitrust law in rare cases demands continued delivery.

Agency agreements can be terminated without cause if contractually agreed. However, mandatory notice periods have to be complied with, staggered pursuant to the contractual term (similar to article 15 (2) Commercial Agency Directive): from one month in the first, two months in the second, three months in the third, fourth and fifth year to six months after five years (section 89(1) HGB). The notice periods cannot be shortened and, in case of extension, the supplier's notice period must not be shorter than the agent's (section 89(2) HGB). A cause is only required if the agreement is terminated without a notice period (section 89a HGB). Such reason exists if the terminating party cannot reasonably be expected to continue the relationship until ordinary termination (considering all circumstances of the single case and weighing the interests of both parties).

Distributor agreements with an indefinite term can be terminated (sections 314, 573, 620(2) and 723 BGB); the notice period depends, however, on the single case, considering also the distributor's investments. For example, one-year periods have been accepted in automotive distribution (BGH, decision of 21 February 1995, *Citroën*). In rare cases, antitrust law may demand a renewal of the relationship.

Franchise agreements can be terminated according to agency law (*mutatis mutandis*). However, longer periods can apply in specific cases, for example, if the franchisee made considerable investments due to the supplier's product.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

The commercial agent is entitled to indemnity if the agent has brought new customers or has significantly increased the business volume with existing customers, which results in benefits for the principal, and if such payment of indemnity is equitable under the given circumstances (section 89b HGB). Indemnity is calculated on basis of the commission earned during the past 12 months of activity, earned with new customers, and existing customers towards whom the agent has substantially increased the sales. Indemnity is capped to a maximum of the past five years' average annual commission (section 89b(2) HGB). The claim cannot be waived before termination, but is excluded if the agent has not notified the principal within one year following termination. Indemnity is not payable if:

- the agent terminated the contract (unless justified by circumstances attributable to the principal or because of the agent's age or illness);
- the principal has terminated the contract because of default attributable to the agent (which would justify immediate termination for cause); or
- the agent, with the principal's agreement, assigns and transfers its rights and duties under the agency contract to another person.

Indemnity cannot be contracted out, unless the agent acts outside the EEA (section 92c HGB). This has been confirmed by the European Court of Justice in its latest ruling on the international scope of the Commercial Agency Directive (decision of 16 February 2017, *Agro Foreign Trade & Agency Ltd/Petersime NV*; cf. Rohrfen, *ZVertriebsR* 2017, 181 et seq). For details on the different levels of protection of commercial agents in various countries, see Rothermel, *Internationales Kauf-, Liefer- und Vertriebsrecht*, 2016, with country overviews in chapter H.

The distributor can claim indemnity only by analogue application of agency law (see question 8). The distributor's indemnity can amount to the distributor's average annual net margin. For a long time, it was disputed whether the distributor's goodwill indemnity could be excluded under German law in advance when the distributor operates outside Germany, but within the EEA. The BGH has recently denied such exclusion, provided the preconditions for analogue application of agency law are given, arguing that agency law restrictions applied here as well by way of analogy, hence in the distributor's favour (BGH, decision of 25 February 2016, *Convection-reflow Soldering Systems*).

The franchisee can likely claim indemnity based on analogue application of agency law, but this has not yet been ruled out (BGH, decision of 23 July 1997, *Benetton*). No indemnity, however, can be claimed where the franchise concerns anonymous bulk business and customers continue to be regular customers only de facto (BGH, decision of 5 February 2015).

The commission agent may also claim indemnity based on analogue application of agency law (BGH, decision of 21 July 2016, *Thomas Philipps*). The claim can probably be avoided, especially by excluding the commission agent's obligation to transfer the customer base to the principal (for details, see Franke/Rohrßen, *IHR* 2017, 62-70).

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

A provision that prohibits the transfer of distribution rights will be enforced (section 399 BGB). Distribution rights are not assignable without the supplier's consent if the supplier has a reasonable interest in the distributor's or agent's personal performance (sections 613 and 664 BGB).

A transfer of ownership (change of control) cannot be hindered. However, the distributor can agree not to transfer ownership, and, in case of breach, the supplier is entitled to damages, including, if possible, re-transfer of ownership (section 137 BGB). In addition, the parties could agree on a termination right in case of change of control.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

Limitations exist, especially as regards the draft of standard business terms. Within such, confidentiality provisions shall clarify the scope of confidentiality (what, who, how long). Contractual penalties may only apply if the receiving party culpably broke confidentiality; the amount of penalty has to be reasonable (sections 310, 307 and 343 BGB and 348 HGB).

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

Non-compete obligations towards distributors and franchisees are enforceable if they conform to antitrust law. Generally, agreements that aim at or result in restraints of competition are prohibited by antitrust law, namely by the German Act Against Restraints of Competition (GWB) and articles 101 and 102 of the Treaty on the Functioning of the European Union (TFEU).

Unless agreements contain hard-core restrictions, a safe harbour is provided by the De Minimis Notice of 30 August 2014 and the Vertical Block Exemption Regulation No. 330/2010 (VBER). Agreements between non-competitors are safe if each party's market share does not exceed 15 per cent on any relevant market affected.

If one party's market share exceeds 15 per cent, but none exceeds 30 per cent, a non-compete obligation during the contractual term is valid if limited to five years at most. Where products are sold on premises owned by the supplier or leased by the supplier from third parties not connected with the buyer, the five-year maximum does not apply. However, the non-compete obligation cannot exceed the term for which the buyer is occupying the premises. After the contractual term, a non-compete obligation where one party's market share exceeds 15 per cent, but none exceeds 30 per cent, is valid if it is necessary to protect

know-how transferred to the distributor, and if limited to competing products, the concrete distributor's premises, and a one-year term.

If one party's market share exceeds 30 per cent, any restriction of competition, including non-compete obligations, can only benefit from the individual exemption under the strict criteria of article 101(3) TFEU (efficiency defence).

Non-compete obligations towards agents are enforceable. Antitrust law generally does not apply, provided that the principal bears the commercial and financial risks related to selling and purchasing the products or services (Guidelines on Vertical Restraints of 10 May 2010, paragraphs 12 et seq, 18 and 49). Special limits apply only to post-contractual non-compete obligations if concluded before termination. They must be limited to a two-year maximum, to the agent's territory or customers, and to the contractual products or services. Further, they must be done in writing and delivered to the agent. The principal has to pay an indemnity for the non-compete obligation's term (section 90a HGB).

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

Generally, a supplier may not fix a resale price or price level at which its distributors or franchisees resell (except for suppliers that manufacture newspapers, magazines and books, section 30 GWB). An agreement or behaviour that aims at establishing such resale price maintenance is treated as a hard-core restriction and therefore generally void (see Guidelines on Vertical Restraints of 10 May 2010, paragraphs 48, 223). By way of exception, the supplier can plead the efficiency defence (eg, when introducing a new product or a coordinated short-term, low-price campaign). However, resale prices can be influenced by recommending resale prices or setting maximum resale prices (see question 15). As regards enforcement, see question 22.

Suppliers can control the price at which they sell the products or services via agents because the antitrust law restrictions do not apply (see question 13).

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

Recommending resale prices or setting maximum resale prices is exempt from antitrust law if the parties' market shares do not exceed 30 per cent (beyond, there is only room for the efficiency defence), and only if it does not result in a minimum or fixed sale price because of pressure or incentives from one party (article 101(1) TFEU and article 4(a) VBER).

Establishing a minimum advertised price policy is exempt if it works as mere recommendation. If, however, it results in minimum resale prices or a fixed or minimum price level, it can only be exempt under the efficiency defence.

By contrast, a supplier shall not announce it will not deal with distributors or franchisees that do not follow its pricing policy because it will be treated as fixing the selling prices (see question 14).

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

A most-favoured nation or most-favoured customer clause is enforceable if agreed between non-competitors and if none of the parties' market shares exceeds 30 per cent (beyond, there is only room for the efficiency defence).

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

Generally, a seller can charge different prices to different customers because of freedom of contract. However, a seller:

- may have to charge the same prices if it holds a dominant or similarly strong market position (sections 19 and 20 GWB and article 102 TFEU); and
- may generally not charge different prices on grounds of race or ethnic origin. The same goes for grounds of gender, religion, disability,

age or sexual orientation if the respective sales contract is typically concluded with or without low importance of the buyer's person, especially in 'bulk business'. An exception exists if different treatment is based on objective grounds, especially where it serves to avoid threats, prevent damage, etc (sections 19 and 20 of the Anti-Discrimination Act).

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

Whether measures restrict competition and are prohibited is to be determined by the antitrust law of the country in which the measures have an effect ('effects doctrine'). Within the European Union or the EEA, a supplier may generally not restrict the territories in which or the customers to whom its distribution partner sells; such restrictions are generally prohibited and void (article 101(1)b, (2) TFEU; article 53 EEA Agreement). Exempt are, however, by reason of block exemption, restrictions of:

- active sales into the exclusive territory or an exclusive customer group reserved to the supplier or another distribution partner;
- sales to end users if the distribution partner operates at wholesale level;
- sales from members of a selective distribution system to unauthorised distributors in the system's territory; and
- selling components, supplied for incorporation, to customers who would use them to manufacture the same kinds of products (article 4(b) VBER).

Active sales means actively approaching individual customers (eg, by direct, unsolicited mail, email or visits) or a customer group in a specific territory through promotions specifically targeted at that group. Passive sales means responding to unsolicited requests from individual customers, including general advertising that reaches customers in other exclusive territories or customer groups if done reasonably.

This also applies to the internet: sales via online stores may not, in principle, be excluded. A supplier may only, however, require its distribution partner to fulfil certain quality standards, especially in selective distribution (Guidelines on Vertical Restraints of 10 May 2010, paragraphs 51 and 54). The European Court of Justice has now shed further light on highly discussed details of internet resale restrictions within selective distribution systems, when deciding on the Higher Regional Court of Frankfurt's request to give a preliminary ruling on how to interpret European antitrust rules, namely article 101 TFEU and article 4(b) and (c) VBER (decision of 19 April 2016, *Coty Germany*, file No. 11 U 96/14 (Kart)). According to the European Court of Justice's decision of 6 December 2017 (*Coty Germany*, reference No. C-230/16), manufacturers of luxury products may stop the distributors within their selective distribution network from selling the goods via third-party platforms if such contractual clause meets the following three conditions: '(i) that clause has the objective of preserving the luxury image of the goods in question; (ii) it is laid down uniformly and not applied in a discriminatory fashion; and (iii) it is proportionate in the light of the objective pursued.' If these 'Metro'-criteria for selective distribution (leading back to the *Metro* case of 25 November 1977, reference No. 26/76) are not met, the clause may nevertheless benefit from an exemption under VBER by reason of article 101(3) TFEU because banning sales via third-party online platforms does not, at least according to the court, under a selective distribution system for luxury goods, constitute a hardcore restriction as listed in article 4 VBER, which would otherwise exclude applying the block exemption to the whole vertical agreement (cf. Guidelines on Vertical Restraints of 10 May 2010, paragraph 47). Especially, the third-party platform ban would not constitute a restriction of customers in terms of article 4(b) VBER, or a restriction of passive sales to end users in terms of article 4(c) VBER. The court left open whether this interpretation also applies for other than luxury goods and outside selective distribution – which will likely be in the centre of discussions now since the German competition authority declared immediately via Twitter on 6 December 2017:

The #ECJ has taken care to limit its findings to genuine luxury products. #Brandmanufacturers have not received carte blanche to issue blanket #platformbans. First assessment: Limited impact on our practice.

The European Commission disagrees: in its Competition Policy Brief of April 2018, the European Commission states – rather incidentally – that the European Court of Justice's argumentation in the *Coty* case also applies irrespective of the luxury character of the products marketed:

The arguments provided by the Court are valid irrespective of the product category concerned (i.e., luxury goods in the case at hand) and are equally applicable to non-luxury products. Whether a platform ban has the object of restricting the territory into which, or the customers to whom the distributor can sell the products or whether it limits the distributor's passive sales can logically not depend on the nature of the product concerned.

Accordingly – as analysed in this guide's 2018 version – the European Court of Justice's decision in the *Coty* case provides good abstract arguments that manufacturers of both luxury and other brand-name products may ban the sale via internet platforms – either according to the 'Metro'-criteria or according to the VBER. In this regard, see, also the recent decision of the Higher Regional Court of Hamburg of 22 March 2018, which held that the ban the producer of food and cosmetics (ie, not luxury goods, but 'but products 'qualitatively committed to a high (production) standard') imposed on its own distributor to sell via third-party internet platforms was valid (for details see Rohrsen, *ZVertriebsR* 2018, 277-285 (281)).

With regard to resale restrictions, the EU Regulation on Geo-blocking (No. 2018/302) prohibits traders to discriminate against customers within the European Union for reasons of nationality, place of residence or place of establishment with regard to the access to online interfaces (article 3) and to the application of general conditions of access to goods or services (article 4). Within the range of means of payment accepted, traders shall not apply different conditions for payment transactions based on nationality, place of residence, place of establishment of the customer, location of the payment account, place of establishment of the payment service provider or place of issue of the payment instrument within the European Union (article 5). Where distribution agreements impose obligations to exercise any form of unjustified geo-blocking as laid down in articles 3, 4 and 5, such provisions shall be automatically void (article 6 (2)). The Regulation on Geo-blocking applies since 3 December 2018. Yet, article 6 (2) shall apply to the agreements on passive sales concluded before 2 March 2018 as from 23 March 2020 only (for details see Rothermel and Schulz, *K&R* 2018, 444-449; Rohrsen, *ZVertriebsR* 2018, 277-285 [283-284]).

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

Yes, a supplier may restrict e-commerce sales by its distribution partners (especially: distributors or franchisees) under German and EU antitrust law – observing the principle that suppliers may hardly impose a comprehensive prohibition on the online sale of goods (or services) because they are considered passive sales (cf. European Court of Justice, decision of 13 October 2011, *Pierre Fabre*, file No. C-439/09, reaffirmed in the case regarding *Coty Germany*, file No. C-230/16; Guidelines on Vertical Restraints of 10 May 2010, paragraph 52; in this regard see also the *Asics* decision of the BGH of 12.12.2017, which states that a general ban on the use of price comparison tools is void, while setting up guidelines for the use of such tools may be valid (see Rohrsen, *ZVertriebsR* 2018, 277-285 (282-283)). Restrictions below a total ban are commonplace, especially the prohibition of sales via third parties' online platforms (especially 'marketplaces'), the ban of pure online players by requiring the operation of brick and mortar shops (Guidelines on Vertical Restraints of 10 May 2010, paragraph 52(c)), or setting quality criteria for internet sales (regarding the domain name, the online store's appearance, the language, the services provided, etc) – (for details, see Rohrsen, *GRUR-Prax* 2018, 39-41 and *DB* 2018, 300-306). Such restrictions within a selective distribution system are either allowed if they meet the 'Metro'-criteria (see question 18) or can be exempt under the VBER – which requires that (i) supplier's and buyer's market shares do not exceed 30 per cent and (ii) that there are no

hardcore restrictions listed in article 4 VBER or excluded restrictions under article 5 VBER.

A supplier may require that e-commerce sales by its distribution partners (not, however, by their customers) are not resold outside the distribution partner's assigned territory, but only as regards active sales into the exclusive territory or an exclusive customer group reserved to the supplier or another distribution partner (see question 18) and only provided that the supplier's and the distribution partner's market shares do not exceed 30 per cent. Passive sales over the internet, that is, upon unsolicited requests from individual customers, can, in principle, not be restricted.

A supplier may require reports of e-commerce sales as a supplier may require reports on any other sales from its distribution partner.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

A supplier may refuse to deal with customers because of freedom of contract, unless restrictions by antitrust or anti-discrimination law apply (see question 17).

A supplier may restrict its distributor's ability to deal with particular customers only if an exemption from antitrust law is given (see question 18).

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

Typically, German or European rules on merger control do not apply to the conclusion of a distribution agreement because such agreement is a form of cooperation between companies different from merger or acquisition. By way of exception, the conclusion of a distribution agreement may be subject to merger control under:

- German law if it is considered a 'combination of undertakings enabling one or several undertakings to exercise directly or indirectly a material competitive influence on another undertaking' (sections 37 et seq GWB). This combination shall, however, only exist if the parties are somehow affiliated; mere economic influence shall not suffice; and
- European law if it results in gaining direct or indirect control of the whole or parts of one or more other undertakings, including by contract (article 3(1b) EC Merger Regulation 139/2004). This control may also exist because of mere economic dependencies (which is to be measured on all circumstances of the case).

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

Generally, agreements that aim at or result in restraints of competition are prohibited by antitrust law (see question 13). Certain hardcore restrictions are generally prohibited, regardless of the parties' market shares, for example, price fixing (see question 14), or restricting the geographic areas or categories of customers (see question 18). Other hard-core restrictions especially apply to selective distribution (eg, no restriction of cross-supplies between distributors within a selective distribution system).

Except for hard-core restrictions, a safe harbour is provided by the De Minimis Notice and VBER (see question 13). If, however, one of the parties' market share exceeds 30 per cent, an agreement or concerted practice that restrains competition can only benefit from the efficiency defence of article 101(3) TFEU.

Antitrust law is mainly enforced by the authorities (the European Commission and the German Federal Cartel Office), especially through fines. However, it can also be enforced by private action, aiming to remove the infringement of antitrust law or achieve damages (sections 33 et seq GWB).

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

A distributor or agent cannot directly prevent parallel imports. Instead, they can only demand from their supplier to use its rights, if existent, to prevent parallel imports. As a general rule, the trademark proprietor of a EU trademark is entitled to prevent all third parties not having his consent from using in the course of trade, in relation to goods or services, any sign identical or similar with the EU trademark (article 9 EU Trade Mark Regulation No. 2017/1001). However, such rights are exhausted 'in relation to goods which have been put on the market in the European Economic Area under that trademark by the proprietor or with his consent' (article 15 (1) EU Trade Mark Regulation). However, the rights are not exhausted if a legitimate reason to prohibit the grey market sales exists, namely because the use of the trademark threatens to damage the good's reputation (as already decided by the Court of Justice of the EU, case C-337/95, *Dior/Evora*). A very recent court decision now confirms that this goes especially for the image of brands that have a luxury and prestige character, as reflected also through how they are advertised. The right to prevent such sales is, however, limited to cases with 'a risk of damage to the reputation', especially where the trademark used by the reseller 'substantially damages' the trademark reputation. The court found that the use of a distribution channel not complying with the selective distribution system caused such reputational damage to the reputation of the luxury cosmetics to be distributed, namely by presenting the products amid other, very standard products for daily use, low priced products and special deals, all not requiring any need for advice to the customers (Higher Regional Court of Düsseldorf, decision of 6 March 2018; details: Rohrßen and Tenkhoff, *GRUR-Prax* 2018, 235).

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

When advertising and marketing products, they generally have to observe the Unfair Competition Act, avoid misleading advertising, adhere to the Ordinance obliging sellers to mark goods with prices, and further provisions that regulate market behaviour in the interest of market participants (eg, labelling of textiles or food products). The parties are free to agree on the cost of advertising.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

A supplier may safeguard its IP by registering its patents, trademarks, utility models, and designs in the territory where the products shall be distributed now or in the future. Thus, the supplier can exert the respective rights in case of infringement. Besides, a supplier may stipulate indemnity clauses in their distributor contracts to cushion the consequences of possible infringements.

Technology-transfer agreements are common and governed by the Technology Transfer Block Exemption Regulation No. 316/2014.

26 What consumer protection laws are relevant to a supplier or distributor?

Above all, consumer protection laws apply at the end of the distribution chain: between the seller and the buying consumer. Statutory law grants a two-year warranty that products are free from defects at the passing of risk. In case of a defect, the buyer is entitled to claim subsequent performance (remedy of the defect or delivery of a defect-free product), alternatively price reduction or withdrawal (all regardless of fault), and damages, provided that the seller has acted with fault (sections 437, 280 et seq BGB). Although fault is generally assumed by law, the seller can exculpate itself, especially if the seller has not manufactured the product. These consumer rights cannot be contracted out by the supplier (sections 474 and 475 BGB).

Each seller within the distribution chain is entitled to have recourse against its own supplier if the product has already been defective at the respective delivery (sections 478 and 479 BGB). In order to maintain these rights, however, the buyer (unless a consumer) has to check at the time of delivery whether the product is defective, and inform the seller accordingly (section 377 HGB).

In addition, special information duties towards consumers exist in:

- over-the-phone sales (section 312a(1) BGB);
- over-the-counter sales, except everyday sales (section 312a(2) BGB, article 246(2) Introductory Act to the Civil Code);
- e-commerce (section 312j BGB); and
- direct distribution off-premises and distance contracts (section 312d BGB).

Statutory law also limits the fees that the consumer shall pay for means of payment or consumer hotlines, etc (section 312a(3–5) BGB). Finally, the consumer has a right of withdrawal regarding distance and off-premises contracts (sections 312g and 355 BGB).

These consumer rights are similar throughout the European Union because they are influenced by the EU Directives 1999/44/EC on the sale of consumer goods and 2011/83/EU on consumer rights. Differences, however, exist, for example, as to whether certain rules also apply within B2B relationships (eg, as regards the seller's obligation to give customers the opportunity to identify and correct input errors before placing their electronic orders).

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

Statutory law does not set any requirements. According to case law, a manufacturer must keep its products under surveillance and, when detecting risks for legally protected goods (such as healthcare products), adopt the necessary preventive measures. The extent and time of such measures depend on the single case, especially on the product at risk and the extent of possible damage (BGH, decision of 16 December 2008).

The distribution agreement can delineate which party is responsible for a recall and its costs. Individual agreements are not subject to specific limits. Standard business terms, however, are subject to a strict review in court: they can be unenforceable if they are incompatible with essential statutory principles, if they limit essential contractual rights and duties, or if they are surprising or ambiguous (sections 310(1), 307, 305c BGB). Therefore, such terms should consider who would typically be responsible for recall and costs, depending on the product (ready-made, or not, etc).

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

A supplier may limit the warranty rights granted by statutory law (see question 26) towards its distribution partners.

There are a few limits to individual agreements: they must not contradict statutory prohibitions (section 134 BGB) and public policy (section 138 BGB), and must not limit or exclude liability for wilful intent, fraudulently concealing defects, where a guarantee has been given, or according to product liability law (sections 202, 276, 444, 639 BGB). If the product has been found to be defective by the consumer, and the defect already existed when the supplier delivered it to its distribution partner, a limitation of warranty can only be enforced if the supplier provides another compensation of equal value (section 478(4) BGB).

In standard business terms, however, one may hardly deviate from statutory law – even in B2B contracts (sections 310(1) and 307 BGB). One may only:

- modify the rules of subsequent performance (time, place, number of attempts);
- exclude liability for slightly negligent breaches of non-cardinal duties; and
- limit liability for slightly negligent breaches of cardinal duties to the typical damages foreseeable at conclusion of the contract.

The same goes for warranties provided to each downstream customer, unless the customer is a consumer because a consumer's statutory rights cannot be contracted out (see question 26).

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

The exchange of information about customers is restricted by the Federal Data Protection Act (BDSG), which implemented EU Directive 95/46/EC, repealed by Regulation (EU) 2016/679 (General Data Protection Regulation or GDPR). The collection, processing and use of information on customers are only allowed if permitted by law (eg, due to the performance of a contract) or with the customer's consent (section 4 BDSG). Details on commercial collection and data storage for the purpose of transfer are laid down in sections 28 et seq BDSG.

The owner of customer information, if contained in a database, is the person who produced the database – provided that its assembly, verification or presentation required a substantial qualitative or quantitative investment (sections 87a et seq of the German Copyright Act).

As regards data transfer from the EEA to the United States, the Safe Harbour privacy principles for the protection of personal data transferred from an EU member state to the United States (Safe Harbour) do not apply anymore. Safe Harbour is invalid owing to the European Court of Justice's *Schrems* decision (6 October 2015). Subsequently, the European Commission and the US government agreed on a new framework for the transatlantic transfer of personal data for commercial purposes. On 12 July 2016, the European Commission adopted the EU-US Privacy Shield. In practice, US companies have to (i) self-certify annually that they meet the requirements, (ii) display privacy policy in their e-stores, and (iii) reply promptly to complaints. If US companies are handling human resources data, they also have to cooperate and comply with European Data Protection Authorities. Details can be found, for example, on www.privacyshield.gov.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

A supplier may generally approve or reject managers if the agent or distributor has to render the services in person (see question 11). However, the distribution partner is free to employ assistants, unless the parties have agreed on a respective 'veto right' for the supplier.

A supplier may terminate the relationship with notice (if of indefinite term, or agreed), or without notice, but for cause (see question 9). Termination for cause, however, requires a more concrete cause than 'missing satisfaction' with the management (unless individually agreed). What might suffice is if culpable mismanagement has resulted in a strong decrease in turnover.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

An agent would be treated as a supplier's employee if the agent does not act independently. An agent acts independently if the agent – according to the overall picture of contractual rules and factual activity – freely organises his or her activities and working time (section 84(1)2 HGB). This goes *mutatis mutandis* for other types of distribution partners.

Treatment as an employee in particular has the following consequences:

- employee protection, for example, limited right of termination under the Dismissal Protection Act;
- continued payment of salary during public holidays, illness and holidays;
- minimum wage under the Minimum Wage Act of 11 August 2014;
- obligation to pay contributions to social security;
- income tax on salary;
- adherence to worker participation and collective bargaining agreements if applicable; and
- exclusive competence of labour courts if the employee has, during the last six months of activity, earned an average amount that does not exceed €1,000 per month.

A supplier generally does not need to protect against responsibility for potential violations of labour and employment laws because the supplier is not required to respond to such violations unless it has

Update and trends

E-commerce

Within the EU's Digital Single Market strategy, the EU intends to remove barriers, eg, by an initiative to simplify contractual rules in e-commerce throughout the EU to open up markets especially for small and medium-sized enterprises (see also the European Commission's press release from 9 December 2015). In May 2016, the EU Commission published a whole e-commerce package, composed of three legislative proposals:

- to address unjustified geo-blocking and other forms of discrimination on the grounds of nationality, residence or establishment;
- on cross-border parcel delivery services to increase the transparency of prices and improve regulatory oversight; and
- to strengthen enforcement of consumers' rights and guidance to clarify, among others, what qualifies as an unfair commercial practice in the digital world.

On 20 November 2017, the European Parliament, the Council and the Commission reached a political agreement to end certain practices of geo-blocking, prohibiting 'three specific situations where no justification and no objective criteria for a different treatment between customers from different EU member states are conceivable from the outset', namely:

- the sale of goods without physical delivery;
- the sale of electronically supplied services; and
- the sale of services provided in a specific physical location (European Commission, Press release of 20 November 2017).

Within two years of the entry into force of the new rules, the Commission will assess for the first time their impact on the internal market, in particular on certain electronically supplied services offering copyright protected content such as downloadable music, e-books, software and online games, as well as on transport and audiovisual services.

For further details, see question 18.

Franchising

There have been discussions about whether to set up statutory rules on franchising in Germany (starting with a petition to the German parliament in 2011). The discussion appears to be petering out on a national level; in December 2015, the Federal Office of Justice announced a one-year research project that shall provide a comparative study of disclosure requirements in countries such as the United States,

France, Spain, Sweden and Belgium. Results are still pending. Whereas on a European level, the discussion is still ongoing: on 12 September 2017, the European Parliament adopted a resolution on the functioning of franchising in the retail sector, inter alia, calling on the Commission to introduce guidelines on franchising contract.

Major trends within distribution and retail

On 10 May 2017, the European Commission published the accompanying Staff Working Document, which set out the main findings of the e-commerce sector inquiry, showing, inter alia, three major trends within distribution and retail:

- direct distribution: Over the past decade, many manufacturers started selling their products directly to consumers through their own online retail shops, thereby competing with their distributors;
- selective distribution: Many manufacturers switched to selective distribution systems, selling their products only to pre-selected (authorised) resellers, thus providing manufacturers a greater control over their distribution networks; and
- rise of contractual restrictions: Together with the rise of selective distribution, manufacturers tend to provide clear criteria to achieve and control the same level of distribution throughout the whole system, including (eg, marketplace (platform) bans, restrictions on the use of price comparison tools and bans of pure online players from distribution networks).

Cross and omni-channel distribution

There is an ongoing trend in distribution from single or multichannel distribution to cross or even omni-channel distribution. The trend is combining all channels to provide customers with a seamless shopping experience, integrating services such as:

- click and collect;
- click and reserve;
- click and deliver; and
- in-store touchpoints.

To avoid frictions within the distribution system, such omni-channel distribution strategy requires clear communication as well as stipulation between the supplier and its distribution partners regarding the use of online stores, social media, local mobile marketing and the coordination and integration of all these services (especially because restrictions on online sales have been under scrutiny by the antitrust authorities in recent times).

contributed to them. However, the supplier can advise the distribution partner in the distribution agreement of the partner's sole responsibility.

32 Is the payment of commission to a commercial agent regulated?

Yes, the agent is entitled to:

- 'del credere commission' if the agent assumes liability for fulfilment of contracts procured by the agent (section 86b HGB);
- an advance on commission once the principal has performed its obligations (section 87a paragraph 1 HGB);
- accounting within maximum periods of three months (section 87c(1) HGB);
- commission irrespective of delivery and payment, unless the principal is not responsible for non-delivery (section 87a(3) HGB); and
- request information, statements of account, an excerpt from the books, and inspection by an auditor (section 87c HGB).

These rules are mandatory and cannot be contracted out. Further details on the payment of commission (if not agreed otherwise) are set out in sections 86b et seq HGB. If a contract procured by the agent is partially not executed, the principal's obligation to pay the commission depends on the concept of 'reason for which the principal is to blame' – as laid down in article 11 of the Commercial Agency Directive and recently interpreted by the European Court of Justice (decision of 17 May 2017, *ERGO Poist'ovňa*): In such a case, the agent may be required to refund a part of his commission, under the conditions that said partial amount is proportionate to the extent to which the contract has not been executed and that the non-execution is not due to a reason for which the principal is to blame (for details see Franke and Rohrßen, *IWRZ* 3/2018, 107-111).

33 What good faith and fair dealing requirements apply to distribution relationships?

The parties to distribution relationships have to safeguard each other's interests (sections 86, 86a and 90 HGB and section 242 BGB).

The agent is especially obliged to:

- check customers' creditworthiness;
- inform the supplier immediately about any business procured;
- keep confidential any information obtained during his or her activity; and
- abstain from acting for the supplier's competitors.

Similar obligations, except non-competition, apply also to distributors, commission agents and franchisees.

The supplier is obliged to assist and take care of its distribution partner, subject, however, to the supplier's economic freedom.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

No.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

German anti-bribery or anti-corruption laws may also apply to the relationship between a supplier and its distribution partner, especially to practices such as:

- taking and giving bribes in commercial practice;
- restricting competition in the context of public invitations to tender; or

- taking or giving bribes to public officials – including inducing or assisting to such acts (sections 298 et seq, 333 et seq German Criminal Code).

Any underlying agreement to such practice can and typically will be declared void as a breach of law (section 138 BGB), for example, an agency agreement that aims at bringing about a bribe agreement with public officials (Higher Regional Court of Stuttgart, decision of 10 February 2010).

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

No (for mandatory provisions, see questions 7 to 10, and 32). The respective statutory law (see question 8) will apply, even if the contract remains silent.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

Generally, the parties are free to choose the applicable law (article 3 of the Rome I Regulation). If, however, all elements relevant for the choice of law are located in another country than that of the chosen law, the choice of law shall not prejudice the provisions that cannot be derogated from by agreement (article 3(3) and (4) of the Rome I Regulation).

Moreover, overriding mandatory provisions of the forum's law cannot be avoided by choosing another law. Similarly, the courts may also give effect to overriding mandatory provisions of the country where the contractual obligations have to be performed (see article 9 of the Rome I Regulation). Overriding mandatory rules are, for example, provisions of agency law. If, therefore, the agent acts within the European Union, the agent's claim for goodwill indemnity (based on the EU Directive on self-employed commercial agents of 1986) cannot be contracted out – even if the parties choose a foreign law (see European Court of Justice, decision of 9 November 2000, *Ingmar*, concerning, however, the former Rome Convention on Law Applicable to Contractual Obligations of 1980). Arguments against applying the same principles under the Rome I Regulation exist, but there is currently no case law that favours that interpretation.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

Generally, the parties are free to choose a court, especially if:

- the other party resides in another EU member state, and the parties have chosen the court of an EU member state (article 25 of the Brussels Ia Regulation);
- the other party resides in Iceland, Switzerland or Norway, and the parties have chosen the courts of one of these states or Germany (article 23 of the Lugano II Convention); or

- both parties are merchants, legal persons under public law, or special assets under public law, or the other party resides outside Germany (section 38 of the Code of Civil Procedure, ZPO).

The parties may instead choose arbitration (sections 1029 et seq ZPO, article 1(2)d of the Brussels Ia Regulation and article 1(2)d of the Lugano II Convention).

However, the choice of court proceedings or arbitration can hardly avoid overriding mandatory provisions (question 37), as ruled by the Higher Regional Court in Munich (decision of 17 May 2006) and confirmed by the BGH (decision of 5 September 2012).

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

Suppliers and distribution partners are free to use any means of dispute resolution, especially out-of-court negotiation, mediation, arbitration or litigation. Restrictions exist only insofar as overriding mandatory provisions cannot be avoided by means of dispute resolution (question 38). Suppliers and distribution partners can expect fair treatment in German courts as the judges are well trained, have been determined beforehand, and the parties are entitled to due process of law (articles 101 and 103 of the German Constitution). The advantages of resolving disputes in Germany are, inter alia, that court rulings are quite foreseeable and that court proceedings are fairly quick (8.2 months on average for proceedings in the district courts, according to the latest statistics).

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

Yes, an agreement to mediate or arbitrate disputes will be enforced in Germany (sections 1029 et seq and section 278a ZPO). Arbitration may be disadvantageous if only small sums are concerned (the costs for German courts are typically lower than the costs for arbitration if the amount in dispute is less than €5 million). Typical advantages of arbitration are, however, that proceedings are confidential, lead to a final decision without the opportunity to appeal, and the award is enforceable in far more countries than court judgments (because of the New York Convention of 1958 on the Recognition and Enforcement of Foreign Arbitral Awards).

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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

Yes, under the same terms and conditions as Greek natural or legal persons. See also questions 3 and 4.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Yes.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

Importers owned by foreign suppliers may carry out business in Greece in a variety of legal forms. Most importantly:

- *sociétés anonymes* (SAs) are regulated by the recently adopted Law No 4548/2018, amending Law No. 2190/1920 and are liable for debts and obligations with their own assets. Shareholders are liable only to the extent of their capital contribution. The minimum capital required is €25,000 (in certain cases, a larger amount may be required). The establishment of the company is completed upon registration with the General Commercial Register;
- limited liability companies are regulated by Law No. 3190/55 and are liable for debts and obligations with their own assets. Their partners are liable only up to the extent of their capital contribution. They resemble partnerships in the way decisions are made since both the majority of the partners and the majority of the capital is required. The capital is determined by the partners (with no restrictions to the amount). All actions necessary for the establishment of a limited liability company are carried out by a notary public. The establishment of the company is completed upon registration with the General Commercial Register. Foreign partners must acquire a tax registration number in Greece;
- private capital companies are regulated by Law No. 4072/2012. Private capital companies are liable for debts and obligations with their own assets. Partners are liable only up to the amount specifically agreed in the articles of association (partners who participate with a guarantee contribution may assume liability for all the company's debts towards third parties up to the amount of their contribution). The capital is determined by the partners and there are no restrictions to the amount. In principle, the articles of association need not take the form of a notarial deed; a private document suffices. The establishment of the company is completed upon registration with the General Commercial Register;
- general partnerships are regulated by Law No. 4072/2012 and the Greek Civil Code. Partners are personally liable for the debts of the partnership without any limitation. There are no minimum capital requirements. The articles of association must be signed before a notary public and are filed with the General Commercial Registry;
- limited partnerships are regulated by Law No. 4072/2012 and the Greek Civil Code. Partners are liable for the debts of the partnership without any limitation except for the limited partner (at least one) whose liability is limited to his or her capital contribution. There are no minimum capital requirements. The articles

of association must be signed before a notary public and are filed with the General Commercial Registry;

- joint ventures (JVs) are not specifically regulated by Greek law. JVs can be subject to corporate law if the parties decide to carry out commercial activities and form a corporate entity which must be registered with the General Commercial Registry (in this case the provisions regulating general partnerships apply); and
- a branch may be registered under Law No. 4548/2018 (as a branch of a foreign SA) or under Law No. 3190/1955, (as a branch of a foreign limited liability company). The branch is administered by an individual (representative) appointed by the foreign company.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

There are no restrictions on foreign suppliers entering the domestic market. The general principles of free movement of goods, persons, services and capital apply in Greece, as a member state of the European Union. See also question 1.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

Yes.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

Foreign companies usually choose to operate in Greece by establishing subsidiaries or branches. The corporate income tax rate in Greece is 29 per cent. Dividends to non-residents are subject to a withholding tax of 15 per cent. No withholding tax applies to dividends paid by a Greek subsidiary to its EU affiliate (under certain conditions, eg, a 10 per cent shareholding is held for an uninterrupted period of 24 months). The same applies to profits that are credited or remitted by a branch in Greece to its head office abroad.

The withholding tax on interest paid to non-residents is 15 per cent, subject to bilateral tax treaty relief.

The tax withheld in Greece for royalties paid to non-residents is 20 per cent, subject to bilateral tax treaty relief.

Payments for services are subject to a 20 per cent withholding tax in Greece (eg, management fees, consultancy fees), unless paid to non-residents with no Greek permanent establishment.

Bilateral tax treaties for the avoidance of double taxation between the country of the supplier and Greece usually regulate all issues regarding the payment of royalties, interest, dividends, capital gains, among others.

A foreign company may be subject to corporate tax in Greece if it obtains 'permanent establishment' in Greece. The provisions of the ITC and the relevant bilateral tax treaties define the term 'permanent establishment'.

Value Added Tax (VAT) in Greece is 24 per cent and applies on the majority of sales of goods and services.

Intra-group transactions must be carried out based on the arm's-length principle (transfer pricing).

A withholding tax is imposed on salaries paid to employees. Moreover, employers must contribute to the social security funds of the employees.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

Commercial agents

A commercial agent acts in the name and on behalf of the principal (supplier) in exchange for an appropriate commission. Agency agreements are regulated by Greek Presidential Decree 219/1991 (PD 219/1991). As per paragraph 2 article 1 of PD 219/1991, the main characteristics of a commercial agency agreement are:

- its bilateral character;
- the permanency of the relationship between the parties;
- the duration of the services rendered by the commercial agent;
- the independence and autonomy of the commercial agent's provision of services; and
- the sale of goods and the rendering of services by the agent on behalf of and in the name of the principal.

Distributors and authorised dealers

A distributor is an intermediary between the producer or supplier of a product and third parties in the distribution or supply chain who purchases the products from the producers or suppliers and undertakes to resell them to third parties acting in his or her own name, on his or her behalf and bearing the associated business risks.

Franchising

Under franchise agreements, the franchisor licenses to franchisees the 'franchise package' which includes, among others, the franchisor's brand name, its know-how, its technical and business methods and so on and supports the franchisee throughout the duration of the franchise agreement. The franchisee undertakes to operate its business following the instructions and assignments of the franchisor.

Commissionaires

Commissionaires are independent merchants whose business consists of buying or selling goods or services (article 90 of the Greek Civil Code) in their own name on behalf of the principal in exchange for an appropriate commission.

Other distribution structures are available to suppliers such as sales representatives (who work in the name and on behalf of their employer), sale under private label, trademark licensing, among others.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

Agency agreements are regulated by Greek Presidential Decree 219/1991 as amended, which implemented the provisions of Council Directive 86/653.

Distribution agreements and franchise agreements are not regulated in Greece by a specific law (see exemption below with regard to exclusive distribution agreements). The parties have a wide discretion in structuring their contractual relationship.

The following laws may also be relevant to distribution or franchise agreements:

- 3959/2011 Greek Competition Act;
- 4072/2012 On Trade Marks;
- 146/1914 On Unfair Competition;
- 2251/1994 On Consumer Protection;
- 2121/1993 On Copyright; and
- the Greek Civil Code.

The provisions of PD 219/1991 may apply, by analogy, to distribution agreements. In particular, article 14, paragraph 4 of Law No. 3557/2007 provides that PD 219/1991 applies to exclusive distribution agreements, in case the distributor acts as part of the sale's organisation of the supplier. However, the above-mentioned law does not refer to other forms of distribution (eg, selective distribution agreements and franchise agreements).

Greek courts have ruled that PD 219/1991 may apply to distribution agreements under the following circumstances (indicatively):

- the distributor acts as part of the sale's organisation of the supplier, having the same weak position and intense dependency on the supplier as the commercial agent, as well as the same degree of integration in the supplier's network;
- the distributor contributes to the extension of the supplier's clientele, undertaking responsibilities similar to those of a commercial agent;
- the distributor undertakes a non-compete obligation;
- the distributor enjoys a specific protected territory; and
- the supplier has knowledge of the distributor's clientele and after the termination of the distribution agreement, the distributor delivers to the supplier a list of its clientele.

The answer to the question of whether PD 219/1991 applies to other forms of distribution agreements (including franchise agreements) needs to be considered on a case-by-case analysis of the 'integration' criteria stipulated above.

There are no government agencies specifically tasked to regulate distribution agreements. However, since competition laws, trademark and unfair competition laws and consumer laws are applicable to distribution agreements, the Hellenic Competition Commission ensures compliance with competition law, the General Secretariat of Commerce or Ministry of Development may address trademark matters, and the General Secretariat of Consumer Protection or Ministry of Development monitors compliance with consumer law in Greece.

There are no industry self-regulatory constraints which could govern distribution agreements. The only exception is the Code of Ethics regarding franchise agreements, a self-regulatory instrument of the Greek Franchise Association. The provisions of the Code of Ethics are compulsory for the members of the Greek Franchise Association, but are not legally enforceable.

Several suppliers and distributors have drafted and implemented their own code of ethics and business morals regarding the distribution of their products.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

The general principles of Greek Civil law apply to the termination of distribution agreements. For fixed-term agreements, termination takes place when the agreed term expires or when there is due cause for termination. Agreements for an indefinite term can be terminated at any time; however, goodwill and other criteria such as the duration of the agreement may impact the validity of termination.

If PD 219/1991 is applicable, article 8 paragraphs 3 and 4 provides that:

where a contract is concluded for an indefinite period either party may terminate it by notice. The period of notice shall be one month for the first year of the contract, two months for the second year commenced, three months for the third year commenced, four months for the fourth year commenced, five months for the fifth year commenced and six months for the sixth year commenced and subsequent years. The parties may not agree on shorter periods of notice.

Moreover, according to article 8, paragraphs 5 and 6 of PD 219/1991:

If the parties agree on longer periods than those laid down in paragraphs 3 & 4 of PD 219/91, the period of notice to be observed by the principal must not be shorter than that to be observed by the commercial agent. Unless otherwise agreed by the parties, the end of the period of notice must coincide with the end of a calendar month.

The above provisions apply in agency agreements.

Agency agreements and distribution agreements that fall within the provisions of PD 219/1991 may be terminated immediately without

the application of the above-mentioned periods of notice, in case one party fails to fulfil all or part of his or her obligations or in exceptional circumstances.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

According to article 9 of PD 219/1991:

the agent, after termination of the agency contract, shall be entitled to an indemnity if and to the extent that he has brought the principal new customers or has significantly increased the volume of business with existing customers and the principal continues to derive substantial benefits from the business with such customers and the payment of this indemnity is equitable having regard to all the circumstances and, in particular, the commission (profits) lost by the distributor on the business transacted with such customers.

The agent must notify the principal to this effect within one year of the termination of the agreement.

Where the agency agreement is terminated for due cause by the supplier, the latter is not liable for such indemnity.

Moreover, the agent shall be entitled to compensation for the damage suffered as a result of the termination, particularly when the termination takes place in circumstances depriving the commercial agent of the commission that proper performance of the agency contract would have procured him or her while providing the principal with substantial benefits linked to the commercial agent's activities, and that have not enabled the agent to amortise the costs and expenses that he or she had incurred for the performance of the agency contract on the principal's advice.

No mandatory compensation or indemnity is required to be paid following termination without cause or otherwise in case the provisions of PD 219/1991 do not apply. However, the distributor shall be entitled to compensation for the damage he or she suffers as a result of the termination of his or her relations with the supplier.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

Yes, if such prohibitions are stipulated in the distribution or agency agreement.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

Confidentiality obligations are, generally, enforceable in Greece.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

Agency

A non-compete obligation is common in agency agreements, throughout their duration and, under article 10 of PD 219/1991, for a reasonable period after the termination of the agreement (one year) and as long as the territory covered by the post-term non-compete obligation is the same as the territory of the expired or terminated agreement.

Distribution

Distribution agreements are subject to Greek and EU competition laws and the rules on restrictive agreements (Law 3959/2011, articles 101 and 102 of the TFEU, Commission Regulation (EU) No. 330/2010 (Block Exemption Regulation – BER) and the related Guidelines).

Non-compete obligations are obligations that require the buyer to purchase from the supplier more than 80 per cent of his or her total purchases during the previous year of the contract goods and services and their substitutes. If one party's market share exceeds 15 per cent, but not 30 per cent, non-compete obligations are permitted when their duration is limited to five years or less. Post-term non-compete obligations normally are not covered by the BER (unless such obligation

is indispensable to protect know-how, the territory covered by the post-term non-compete obligation is the same as the territory of the expired or terminated agreement, and is limited to a maximum one-year period). If the supplier prevents his or her distributors from buying products for resale from specific competing suppliers, such an obligation cannot enjoy the benefit of the BER. If one party's market share exceeds 30 per cent, non-compete obligations can only benefit from the individual exemption under the strict criteria of article 101(3) TFEU ('efficiency defence'). (Guidelines on Vertical Restraints of 10 May 2010, section III, paragraph 5(66).)

Moreover, a non-compete clause in a distribution agreement maybe an indication that PD 219/1991 applies and, therefore, the restrictions stipulated above (agency agreement) will prevail.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

Distribution

Resale price maintenance (RPM), namely agreements or concerted practices having as their direct or indirect object the establishment of a fixed or minimum resale price, is a hardcore restriction (article 4(a) BER). In the case of contractual provisions directly setting resale price, the restriction is clear cut. By way of exception, the supplier can plead the efficiency defence. The provision of a list of recommended prices or maximum prices by the supplier to the buyer is not considered in itself as leading to RPM. (Guidelines on Vertical Restraints of 10 May 2010, section III, paragraph 3(48).)

As regards enforcement, see question 20.

Agency

In agency agreements, the principal normally establishes the sales price. However, if an agency agreement falls within article 101(1) TFEU, namely in case the agent bears the risks in relation to the contracts concluded or negotiated on behalf of the principal and in relation to market-specific investments for that field of activity (non-genuine agency agreement), an obligation restricting the agent from sharing his or her commission with the customer would be a hardcore restriction under article 4(a) BER.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

Distribution

If the supplier provides the distributor with a list of recommended or maximum prices, this (in general) would not lead to RPM. However, indirect means, that is, fixing a maximum discount for a given price 'level', subjecting rebates to the observance of a given price level, and establishing 'supportive' measures, such as an implementation monitoring system, can be used to make maximum or recommended prices work as RPM and, therefore, fall within article 4(a) BER. (Guidelines on Vertical Restraints of 10 May 2010, Section III, paragraph 3(48).)

Agency

The principal normally establishes the sales price, as the agent does not become the owner of the goods (see exemption in question 14).

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

Distribution

Price relationship agreements include clauses whereby a seller's price is related to another price (that is, the price offered by other sellers for the same product or the prices offered by the same seller for the same product to other buyers). Across-customers agreements are agreements whereby the seller agrees to tie the price it charges to the buyer or distributor to the prices it offers to other clients. Across-customers policies may raise competition law issues depending on the nature of the seller who offers it, the characteristics of the market affected and the specificities of the relevant agreement.

Agency

See question 14.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

Generally, sellers may charge different prices to different customers. However, this differentiation cannot be discriminatory, especially in the case of a selective distribution system or when the supplier enjoys dominance in the relevant market.

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

Agreements having as their direct or indirect object territorial restriction of sales by the buyer are listed in the hardcore restrictions of article 4(b) BER. There are four exceptions, as stipulated at the Guidelines on Vertical Restraints of 10 May 2010, section III, paragraph 3(50):

- a supplier may restrict active sales by his or her direct buyers to a territory or a customer group that has been allocated exclusively to another buyer or which the supplier has reserved to itself;
- a wholesaler may be restricted from selling to end users;
- an appointed distributor in a selective distribution system may be restricted from selling, at any level of trade, to unauthorised distributors in markets where such a system is operated; and
- a buyer of components supplied for incorporation may be restricted from reselling them to competitors of the supplier.

'Active' sales mean actively approaching individual customers or a specific customer group or customers inside another distributor's exclusive territory or exclusive customer group. 'Passive' sales mean responding to unsolicited requests from individual customers, including delivery of goods or services to such customers.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

Internet sales are not considered 'active sales' into other distributor's exclusive territories or customer groups and may not be restricted or prohibited. If a customer visits a distributor's site and purchases a product, this would qualify as a 'passive sale'. On the other hand, unsolicited emails sent to individual customers qualify as 'active sales'. In any case, the supplier may impose quality standards for e-shops, just as for physical shops. An outright ban on internet selling is only possible if there is an objective justification.

An agreement whereby the distributor shall pay a higher price for products intended to be resold online than for products intended to be resold offline is considered a hardcore restriction (passive selling) since it can limit the distributor's access to customers. However, the supplier may agree with the distributor a fixed fee to support the distributor's offline or online sales.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

A supplier may refuse to deal with particular customers. However, competition law issues may arise if such refusal has no valid justification and leads to discriminatory behaviour towards customers. Refusal to supply may also be prohibited when the supplier has a dominant position (article 2 of Greek Law 3959/2011).

See question 19 regarding restriction of a distributor's ability to deal with particular customers.

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

A distribution or agency agreement is a vertical agreement. Merger control rules may apply if such relation confers control over another company (control of production, distribution, etc). The competent authority must undertake a thorough analysis to assess whether the

transaction is compatible with effective competition in the relevant market.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

Competition in the Greek market is primarily protected under Law No. 3959/2011 of the Greek Competition Act, which aims at ensuring effective competition. Article 1, paragraph 1 of Law No. 3959/2011 lists the agreements that have as their object or effect the prevention, restriction or distortion of competition in the Greek territory and are prohibited (price fixing, limitation of production or markets, market sharing, discriminatory behaviour, etc). The prohibition captures both horizontal and vertical agreements. Article 1, paragraph 3 provides for the efficiency defence.

As regards vertical agreements, Commission Regulation (EU) No. 330/2010 (the Block Exemption Regulation) and the related Guidelines apply in Greece, with exclusivity, resale price maintenance, product ties and restriction of passive sales constituting the main points of concern. As for the vertical restraints on the purchase, sale and resale of goods and services within a distribution agreement, the BER applies up to the 30 per cent market share threshold.

Competition law is mainly enforced by the Hellenic Competition Commission (HCC) (and the European Competition Commission). The sectors that attract the HCC's attention are defined in line with its applicable priority system. The law provides for fines upon the violating undertakings and criminal sanctions. Persons harmed owing to breach of competition rules may initiate civil proceedings for damages. Despite the lapse of the implementation date, at present Greece has not transposed the EU Damages Directive.

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

In line with EU law, the Greek legal order recognises the EU-wide doctrine of IP exhaustion. IP owners in Greece may rely on such rights to prevent imports of genuine goods from outside the EEA. Intra-EEA parallel imports cannot be prohibited.

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

See question 18.

Advertising and marketing of products are addressed by the Unfair Competition Act (146/1914) that regulates all matters regarding misleading advertising, defamation, exploitation of other parties' goodwill and infringement of third parties' distinctive marks, among others, the Consumer Protection Law (2251/94 as amended) (see question 26) and the relevant Market Regulation Code that regulates all matters relating to prices, advertising, labelling and so on.

The parties are free to agree on the cost of advertising.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

Suppliers may safeguard their intellectual property primarily via registration thereof, where applicable, in Greece, the European Union or internationally designating Greece or the EU. Inclusion of appropriate contractual clauses with local distributors is also a sound strategy, particularly as regards non-registrable IP, for example, copyright or trade secrets.

Technology transfer agreements are not uncommon in Greece.

26 What consumer protection laws are relevant to a supplier or distributor?

The basic consumer protection legislation in Greece is Law No. 2251/1994. It regulates various consumer issues, such as general terms and conditions in consumer contracts, distance selling,

product safe use information obligations, mandatory guarantees and after-sales service, misleading and comparative advertising, product liability, unfair commercial practices and so on.

E-commerce is regulated under Presidential Decree 131/2003, transposing Directive 2000/31/EC. As this piece of legislation regulates only partially the commercial relationship between the seller or supplier of goods or services and the purchaser or user, all other aspects of this same commercial relationship are regulated by the provisions of the Greek Civil Code, as well as by the legislation for protection of consumers, manufacturer's product liability and unfair competition.

Finally, the Code of Consumer Ethics regarding e-commerce sets out the principles and defines the minimum rules of business ethics that suppliers and distributors should preserve towards consumers.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

Article 540 paragraph 1(i) of the Greek Civil Code provides that, in case of liability of the seller for a product defect or if the product is not fit for purpose and, in general, when the product does not comply with the pre-agreed terms of the sale agreement, the buyer can request from the seller the recall of the product and either the repair of its defect or replacement with a new one.

Moreover, article 7 paragraph 6 of Law No. 2251/1994 provides that products that may entail serious and direct risk to consumers' safety and health (even if they are used in normal circumstances) should be recalled by the producer or may be confiscated by the authorities.

The distribution agreement can delineate which party is responsible for a recall and its costs.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

Articles 534 to 561 of the Greek Civil Code provide that the seller (supplier or distributor) is liable for product defects and lack of the agreed product attributes. The buyer (distributor or downstream customer) may claim such liability within two years for movables and five years for immovables of the day of delivery.

Law No. 2251/1994 offers end consumers a right to a minimum guarantee of two years on goods. The seller is obliged to provide the consumer in writing with all the information about the safe use and preservation of the product. The provisions of Law No. 2251/1994 relating to guarantees are mandatory law.

Any additional rights offered by a guarantee from a seller are supplementary to the rights as provided by legislation.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

Until 25 May 2018, Law 2472/1997 on the Protection of Individuals with regards to the Processing of Personal Data (transporting Directive 95/46/EC) was in force. As of 25 May 2018, the General Data Protection Regulation 2016/679/EE (GDPR), which prevails over Law 2472/1997, is in effect. A law implementing the GDPR and transferring Directive 2016/680 has been submitted to public consultation but not adopted yet. In addition, further guidelines on GDPR implementation are expected to be published by the Hellenic Data Protection Authority.

The Hellenic Data Protection Authority (HDPa) is responsible for overseeing Data Protection.

The GDPR refers to data controllers and processors within the European Union and outside the European Union if their processing or monitoring activities relate to the offering of goods and services to EU citizens or data subjects. In certain circumstances, data controllers and processors must designate a data protection officer as part of their accountability obligations to demonstrate compliance. Data processors must maintain a written record of processing activities on behalf of each controller, appoint a representative in certain circumstances and notify the controller if they become aware of a personal data breach.

A data subject's consent must be free, specific, informed, unambiguous and easy to withdraw and to give. Data controllers must continue

to provide transparent information to data subjects and notify data breaches to the HDPa. Moreover, a significant change for data controllers is the removal of the general requirement to notify the HDPa of a controller's data processing activities and seek approval in specific circumstances.

In distribution agreements, the distributor is generally the owner of the information. The transfer of personal data is permitted for EU member states and for non-members of the European Union on the basis of an adequacy decision of the European Commission. The transfer of personal data to a non-member state of the EU that does not ensure an adequate level of protection is allowed, following authorisation by the HDPa, under exceptional conditions, including where the data subject has consented to the transfer and the transfer is necessary to protect the vital interests of the data subject.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

Yes, such provisions are common in distribution agreements.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

Suppliers and distributors are regarded as separate, independent business partners. If the distributor is in control of its business, sells the products in its own name and for its own account, and controls its sale prices and working hours, the chances that it may be considered as an employee are limited.

However, under certain circumstances, the distributor or agent may be deemed to be the supplier's employee and the Greek employment law could apply, for example, if the distributor or agent is financially dependent on the supplier or has no employees and the supplier is its only supplier, or the degree of supervision of the distributor or agent and its employees by the supplier goes beyond what is necessary.

Qualifying as an employee has consequences regarding protection in case of termination of the agreement, payroll, working time limits, payment of social security contributions, participation in the collective labour agreements and so on.

A distributor cannot be held liable for potential violations of labour and employment laws by its distribution partner.

32 Is the payment of commission to a commercial agent regulated?

Yes. According to articles 5 and 6 of PD 219/1991:

a commercial agent shall be entitled to the remuneration that commercial agents appointed for the goods forming the subject of his agency contract are customarily allowed in the place where he carries on his activities. If there is no such customary practice a commercial agent shall be entitled to reasonable remuneration taking into account all the aspects of the transaction.

A commercial agent shall be entitled to commission on commercial transactions concluded during the period covered by the agency contract where the transaction has been concluded as a result of his or her action; or where the transaction is concluded with a third party whom he or she has previously acquired as a customer for transactions of the same kind. Under article 7(1) of the PD 219/1991, the commission is due as soon as and to the extent that one of the following occurs: (i) the principal has executed the transaction; (ii) the principal should, according to his or her agreement with the third party, have executed the transaction; and (iii) the third party has executed the transaction.

33 What good faith and fair dealing requirements apply to distribution relationships?

Distribution

Under article 288 of the Greek Civil Code, parties must fulfil their contractual obligations 'in good faith' and in 'established fair trade practices'. Good faith is a binding criterion in assessing the conduct of the contracting parties in a distribution agreement.

Agency

In performing his or her activities, a commercial agent must consider the principal's interests and act dutifully and in good faith, namely make appropriate efforts to negotiate and conclude the relevant transactions, communicate to the principal all necessary information available to him or her and comply with reasonable instructions given by his or her principal. The principal must also act dutifully and in good faith vis-à-vis the commercial agent.

Franchise

Under the Code of Ethics, both the franchisor and the franchisee must act fairly, reasonably and in good faith not only during the term of the franchise agreement but also during the pre-contractual phase and post-termination.

In cases of culpable breach of this obligation, the aggrieved party may be entitled to damages.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

To the extent that a distribution agreement includes licensing or transfer of IP rights, the agreement (or a short-form agreement) will need to be registered with the competent IP authority – the Greek Trademark Office for trademark licences or the Greek Industrial Property Organisation for designs or patent licensing and transfer of know-how. There is a specific Technology Transfer Register maintained by the Greek Industrial Property Organisation, according to Law No. 1733/1987.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

There is no specific, distribution-related legislation on prevention of fraud, anti-corruption and money laundering in Greece.

The main regulatory instrument on fraud (and other fraud-related offences) is the Greek Criminal Code (GCC). Moreover, article 237B of the GCC punishes bribery in business or commercial activities.

The basic legal instrument against money laundering and terrorist financing is Law No. 3691/2008, which is in line with relevant international conventions.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

Mandatory provisions relating to distribution or agency agreements are analysed under questions 12 to 35.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

As regards the applicable law, Greek courts recognise the choice of foreign law on distribution agreements regarding a business operating in Greece. However, certain Greek law provisions may apply, despite the choice of the foreign law. Such provisions relate to the protection of Greek public policy, but also competition law, labour law, tax law, data protection law, among others.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

There are no restrictions on the parties' contractual choice of courts or arbitration tribunals.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

The vast majority of cases in Greece are resolved in court. A smaller fraction of disputes are resolved through arbitration, while the recently introduced method of mediation in commercial disputes is still not common.

The remedies provided by Greek law in case of violation of the terms of a distribution agreement by either party are:

- preliminary and definitive injunctions;
- seizure of assets;
- disclosure of financial records;
- pecuniary or non-pecuniary damages; and
- threat of pecuniary penalties in case of future violation of the court's order.

Criminal action may also be initiated in certain circumstances.

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

Greek law provides for two different categories of rules, to apply to domestic and international arbitration respectively.

International commercial arbitration proceedings are governed by Law No. 2735/1999 on International Commercial Arbitration, which incorporates the UNCITRAL Model Law in the Greek legal system.

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Articles 867 to 903 of the Greek Civil Procedure Code regulate domestic arbitration.

The Greek legal framework is supplemented by numerous international conventions, such as the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958).

In general, parties are free to decide on the procedural rules of the arbitration subject to mandatory rules of the law. An arbitral award is not subject to appeal.

A foreign arbitral award is recognised automatically in Greece, provided that the recognition requirements set out in article IV paragraph 1 of the New York Convention are met and none of the grounds for refusal referred to in article V of the Convention exists. Awards in domestic arbitration are recognised and enforced in the same way as the decisions of the national courts.

The recently adopted Law No. 4512/2018 provides for compulsory mediation procedure for certain types of disputes, including trademarks and patents disputes. Following suspension of the initial effective date, compulsory mediation shall be effective as from 16 September 2019.

India

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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

A foreign supplier can establish its own entity in India in order to import and distribute its products by incorporating a private limited company, a public limited company or a limited liability partnership (LLP) as may be appropriate.

Where a foreign company wants to have complete control over all aspects of the business in India and intends to be in India for the long term, a wholly owned subsidiary is recommended. However, the extent of foreign equity participation and control depends upon the exact nature of business in India, and is governed by the foreign direct investment (FDI) Policy of the government.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

A foreign supplier can be a partial owner or equity shareholder in an Indian company with a local partner. Accordingly, a foreign company may form a joint venture in India with any local company, subject to compliance with the FDI Policy. Typically, a foreign supplier chooses to enter into the Indian market by way of forming a joint venture with a local company in order to use the local market expertise and network of the Indian partner.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

Generally, a private limited company is formed as per the procedure laid down under the (Indian) Companies Act 2013 and the rules made thereunder. The corporate affairs of the company are governed and managed as per the provisions of the Companies Act 2013. Further, a company is subject to tax laws in India, and product specific laws are also applicable for importing and distributing products in India.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

Foreign investment in India is regulated and governed by the FDI Policy, which is issued from time to time. Generally, foreign investment in most business sectors is allowed up to 100 per cent under the automatic route; that is, without any prior permission from the government of India or the Reserve Bank of India. However, for certain businesses, the FDI Policy prescribes limits for foreign investment and certain business-related conditions that have to be met by the Indian company that has such foreign investment. For example, a 100 per cent foreign investment or ownership in an Indian company carrying out wholesale trading business in India is allowed under the automatic route. However, for a company engaged in retail activities, different conditions are prescribed for different levels of foreign investment.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

As explained under questions 1, 2 and 4, a foreign supplier can own equity interest in the local entity in India that distributes its products.

The limit of investment depends upon the actual activities to be carried out by the Indian entity.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

The major tax considerations for foreign suppliers in India are corporate income tax, and the treatment of tax incidence under the Double Taxation Avoidance Agreement (if applicable in relation to the supply) entered into between India and the country of the supplier. Several other taxes must also be considered, such as the Goods and Services Tax (GST) (which would be applicable on the sale of goods and services), and customs duty (for import of the supplied products) among others. In relation to owning interests or shareholding in the local business in India, dividend distribution tax (payable at the time of payment of dividend by the Indian company), and capital gains tax (payable by the foreign investor at the time of selling its shares held in the Indian company) become applicable.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

Multiple structures are available to a foreign supplier for distribution of products in India and the same can be chosen based on the commercial objectives and the nature of products of the foreign supplier.

Distributors

Foreign suppliers generally appoint a distributor for the whole of India, or for a certain defined territory, by way of entering into a detailed distribution agreement. Sometimes, the foreign supplier establishes its own entity to act as importer and master distributor in India, and the master distributor further appoints distributors for different territories in India. The suitability of the distributor model depends upon the level of control the foreign supplier wishes to have on the distribution and sales activities in India. Competition law-related issues are important considerations for deciding the distribution structure, such as the fixing of resale price, exclusivity, territorial restrictions, among others.

Agency

The supplier can appoint agents, wherein the supplier is the principal and would retain control over the product sale and price. The agent only represents the supplier in India. Further, the supplier would be legally responsible for all the acts done by the agent in the course of business. The agent is generally not implicated in any financial risk, and all the risks associated with the product rest with the supplier. The agent is paid its commission based on sales made. Agents can have varying authority as per the contract entered into between the supplier and the agent. There are a few products where the appointment of an authorised agent in India is legally required, such as for pharmaceutical drugs and some medical devices.

Franchise

A foreign supplier may adopt a franchise arrangement to distribute its products in India. The said arrangement is generally adopted where

sharing of technical know-how and business methods is required. In India, many foreign suppliers have adopted the franchise model to sell their products.

Other forms of business models

Multinational brands generally enter the Indian market through distributors or franchisees, by formulating an agreement. This concept is usually adopted by new entrants to access the Indian market without establishing their own entities.

Foreign suppliers can also enter into a trademark licensing agreement, whereby they would license their trademark on receipt of the negotiated payments from the licensee. In such an arrangement, generally, the products are manufactured in India, and a royalty fee is paid on the products. The objective is to allow the Indian company to render services or manufacture goods under the foreign supplier's trademark as per the trademark licence agreement.

Companies sometimes opt for a strategic alliance by entering into joint ventures with Indian partners. Strategic alliances are typically adopted by foreign suppliers when local expertise or support of an Indian partner is required for the foreign suppliers to cater to the Indian market in an effective manner, or where there are other synergies of business.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

The relationship between a supplier and distributor is primarily governed by the contract entered into between the parties. The Indian Contract Act 1872 (Contract Act) governs the fundamental principles of the contract. There is no government agency that regulates the entire relationship between the foreign supplier and Indian distributor. However, certain government agencies have regulatory roles based on the specific legal issues where the government agency has a legislative mandate to enforce any specific law. For example, issues related to competition law under a contract are enforced by the Competition Commission of India (CCI), which ensures that any contractual arrangement between the parties does not lead to any appreciable adverse effect on competition in the relevant Indian market or creates any barriers to new entrants or forecloses competition and such like.

Similarly, the provisions of the Foreign Exchange Management Act 1999 (FEMA) are attracted whenever there is involvement of foreign currency and payment-related issues for import of goods into India. The regulatory authority in this regard is the Reserve Bank of India. Further, issues pertaining to warranties, transfer of risks and ownership of goods are governed by the provisions of the Sale of Goods Act 1930. The quality of goods and trade practices are governed by the Consumer Protection Act 1986, which provides for various safeguards against unfair trade practices, defects in goods and deficiency in services.

To ensure the proper use of the intellectual property of the foreign supplier, the provisions of the Trade Marks Act 1999 and the Patents Act 1970 are of relevance.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

There is no legal prohibition on a supplier terminating a contract unilaterally without any reasons, if the contract provides for the same. The right of termination of a contract and the conditions therefor are governed by the terms of the contract between the parties. The distributor agreement usually stipulates the terms and conditions under which the parties to the contract may terminate the contract. Typically, the contract provides for termination right of a party during the subsistence of the contract for any breach of material obligations, misrepresentation, omission or commission of certain acts, infringement of intellectual property and so on. Care should be taken to incorporate reasonable terms for termination of the contract by a party; otherwise the affected party generally tends to challenge the termination of contract on the ground of unreasonableness. However, generally, the courts in India

respect and uphold the contractual terms, if the contract is not totally unbiased.

Contract termination without cause is permitted in India, provided that the terminating party gives a reasonable notice or compensation to the other party. The supplier is under no legal obligation to renew the contract after the contract terminates by passage of time. Indian courts have held that even in the absence of a termination clause in the contract enabling either party to terminate the agreement, the contract can be terminated even without assigning any reason and by serving a reasonable notice or paying compensation in lieu of notice.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

The termination of contract by either party with or without cause does not statutorily require a party to pay any compensation or indemnity to the other party. Compensation or indemnity is paid by the party terminating the contract only in the event that the contract was terminated unlawfully or in contravention of the terms and conditions stipulated under the contract. In the event that the contract is terminated unlawfully or in contravention of the terms and conditions of the contract, then the compensation or indemnity is paid in accordance with the terms of the contract, and in the absence of any express agreement for the same, the compensation amount is determined by the courts.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

The parties to the contract can formulate any terms and conditions within the ambit of the Contract Act, and the courts may enforce a provision prohibiting the transfer of the distribution rights to the supplier's products. The Supreme Court, in the case of *M/s Gujarat Bottling Co Ltd and Others v The Coca Cola Company and Others*, has observed that franchise agreements usually incorporate a condition that the franchisee shall not deal with competing goods. Such a condition restricting the right of the franchisee to deal with competing goods is for facilitating the distribution of the goods of the franchiser and it cannot be regarded as restraint of trade. The restriction on transfer of all or part of the ownership of a distributor or an agent to a third party after the termination of contract may not be enforceable, as the prudence for enforcement of such provisions in India is that no party can restrain the other party from trading, and only a reasonable restriction can be imposed.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

Confidentiality provisions in agreements, during and after the term of such agreements, are generally enforceable in India provided the agreement does not restrain anyone from exercising a lawful profession, trade or business of any kind.

There is no specific legislation to protect confidential information. However, the courts have upheld protection of such information on the basis of the terms and conditions of the contract, and principles of equity and common law action for breach of confidence.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

Indian courts have drawn a clear distinction between non-compete covenants after the term of the agreement and non-compete covenants post the term of an agreement. To determine enforceability of such covenants, the courts consider the question whether the covenant is or is not in restraint of trade.

It is well established that the non-compete covenants operative during the period of a contract are generally enforceable if the restriction is reasonable in the context of the particular trade and business, and where the restriction is required to enhance the level of service to the customers and efficiently manage the sale of products.

In a recent judgment of the Delhi High Court, where there is a reference to franchise agreements for distribution of goods and services,

it has been observed that certain agreements often incorporate terms restricting the rights of the franchisee to deal with competing goods for facilitating the distribution of the goods of the franchiser, and this cannot be regarded as a restraint of trade.

Non-compete covenants, after the expiry or termination of the contract, are generally difficult to enforce as they are considered as a restraint in exercising a lawful profession, trade or business. An exception to this restriction is an agreement not to carry on a business of which the goodwill is sold.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

Control of the resale price by a supplier is generally considered as an anticompetitive agreement, if the same causes, or is likely to cause, an appreciable adverse effect on competition in India. In terms of the (Indian) Competition Act 2002 (Competition Act), agreements between parties to sell goods at different stages or levels of the production chain in different markets on the condition that the prices to be charged on the resale by the distributor or purchaser shall be the prices prescribed by the supplier or seller, are anticompetitive agreements and shall be void if they cause, or are likely to cause, an 'appreciable adverse effect on competition' (AAEC) in India. Such a provision is referred to as 'resale price maintenance' (RPM). However, the exception to this restriction is if the agreement clearly states that prices lower than those stipulated by the seller may be charged.

The AAEC needs to be determined on the basis of the factors provided under the Competition Act. In cases relating to RPM issues, the CCI has used the market share of the product in question as the centrepiece in its analysis and has found that where the market in question was generally competitive, the RPM was less likely to cause an AAEC in India.

Therefore, a supplier can control the prices at which its distribution partner resells its products in India, provided the terms of the agreement and price control mechanism are in compliance with the provisions of the Competition Act.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

A supplier can influence resale prices by suggesting resale prices, establishing a minimum advertised price policy both for physical or online sale, or by announcing that it will not deal with customers who do not follow its pricing policy or such like, if such agreement includes the exception provided in the Competition Act in the case of RPM, and if the terms of pricing do not cause, or are not likely to cause, AAEC under the Competition Act for the given market or products.

Care should also be taken that the provision related to refusal to deal should not amount to abuse of dominant position by the seller under the Competition Act.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

Yes, such a provision can be incorporated in the distribution contract, provided that such restriction does not amount to creating an AAEC in the relevant market in India.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

Generally, a seller can charge different prices to different customers based on location, type of customer, quantities purchased or otherwise. There is no legal restriction for the same. However, in the event that the seller is a foreign company and the distributors are based in India, and if different distributors import the goods at different prices, the issue relating to evasion of customs duty by the distributor importing at a lower price may arise. The issue would not be relevant where the Indian entity of the foreign seller imports into India and thereafter distributes its products to different distributors in India at different prices based on location, type of customer, quantities purchased, or otherwise.

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

Generally, an exclusive distribution agreement, including an agreement that limits, restricts or withholds the output or supply of any goods or allocates any area or market for the sale of the goods, is considered as an anticompetitive agreement, if such agreement causes, or is likely to cause, an AAEC in India. However, the Competition Act provides for an exception where such restriction is necessary for restraining any infringement of, or to protect, intellectual property rights.

Matters related to anticompetitive agreements are decided on a case-to-case basis on the basis of the rule of reason, which involves enquiry into the purpose and effects of an agreement, whether the restraint imposed is such that it merely regulates and perhaps promotes competition, or whether it is such that it may suppress or even destroy competition.

Therefore, a supplier can restrict the geographical area or categories of customers if the agreement is in compliance with the above provisions of competition law.

The concept of active sales efforts and passive sales are not recognised under Indian law. Restrictions, whether express or implied, are tested on the touchstone of the above legal principles.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

Considering the views taken by the CCI while dealing with various complaints made against e-commerce websites in India, it can be concluded that offline and online markets are not two different relevant markets, and are only different channels of distribution of the same product. E-commerce entities need to maintain a level playing field. Therefore, the legal position relating to the suppliers' restriction on e-commerce sales by its distributors would be the same as explained in question 18 and would be considered under the category of exclusive distribution agreement. Accordingly, such restrictive covenants in the agreement may amount to being anticompetitive if the agreement causes, or is likely to cause, an AAEC in India.

As explained above, these cases are decided on their own specific facts, on the basis of the rule of reason, which involves enquiry into the purpose and effects of an agreement, whether the restraint imposed is in any manner reducing competition in India, or merely regulates and promotes competition. In such a case, restriction can be provided for in the agreement.

Any provision stating that e-commerce sales by distribution partners, or by e-commerce intermediaries to which the distribution partner sells, are not resold outside the distribution partner's assigned territory may be included, if it can be proved that the agreement does not cause, or is not likely to cause, an AAEC in India.

Further, there is no restriction on the supplier to require reports of such sales by territory. A provision for claiming 'invasion fees' or similar amount by the distribution partner may be incorporated in the distribution agreement, if such exclusive distribution agreement is not considered void under competition law.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

Yes, a supplier can refuse to deal with particular customers; however, restricting its distributor's ability to deal with particular customers under contract may be treated as an anticompetitive agreement if the agreement causes, or is likely to cause, an AAEC in India.

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

As per the Competition Act, no distribution or agency agreement is required to be reported under the merger control regulation or require clearance by the CCI. However, the CCI may, on the basis of any

complaint made before it or on its own motion, initiate an inquiry if it comes to the knowledge of the CCI that any agreement is an anticompetitive agreement and such a transaction is likely to cause an AAEC in the relevant market in India.

To evaluate the AAEC, the CCI, among others, considers the following factors:

- creation of barriers to new entrants in the market;
- driving existing competitors out of the market;
- foreclosure of competition by hindering entry into the market;
- accrual of benefits to consumers;
- improvements in production or distribution of goods or provision of services; and
- promotion of technical, scientific and economic development by means of production or distribution of goods or provision of services.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

The competition laws of India regulate the relationship between suppliers and their distributors. In addition to the restrictions and regulations stated above, the competition laws prohibit the following agreements:

- any agreement in respect of production, supply, distribution, storage, acquisition or control of goods, which causes, or is likely to cause, an AAEC in India;
- any agreement which, directly or indirectly, determines purchase or sale prices, limits or controls production, supply, markets, technical development, shares the market or source of production by way of allocation of geographical area of market or type of goods or number of customers in the market; and
- tie-in arrangement, exclusive supply agreement, exclusive distribution agreement, agreement for refusal to deal, resale price maintenance and so on, if such agreement causes, or is likely to cause, an AAEC in India.

However, the above restrictions are not applicable where any agreement entered into by way of a joint venture, if such agreements increase efficiency in production, supply, distribution, storage, acquisition or control of goods or for the purposes of protecting intellectual property rights.

Further, any agreement resulting in abuse of dominant position by a party whereby the agreement imposes unfair or discriminatory conditions in the purchase or sale of goods, or places restrictions on prices, limits or restricts the market, results in denial of market access, or makes the conclusion of contracts subject to acceptance of supplementary obligations (which, by their nature or according to commercial usage, have no connection with the subject of such contracts), is not permissible under the competition laws of India.

Competition law matters are dealt with by the CCI, as per the procedure provided under the Competition Act, to determine anticompetitive agreements and abuse of dominant position as provided in the Competition Act.

On completion of an inquiry in the manner prescribed under the Competition Act, the CCI has the power to pass any or all of the following orders:

- impose a penalty;
- direct modification of the agreements;
- pass an interim order to temporarily restrain any party from carrying on such act until the conclusion of the inquiry, or until further orders;
- discontinue and not to re-enter such agreement, or discontinue the abuse of dominant position, as the case may be; direct division of an enterprise enjoying dominant position to ensure that the enterprise does not abuse its dominant position;
- direct the enterprises concerned to abide by such other orders as the CCI may pass and comply with the directions, including payment of costs, if any; and
- pass any other order as it may deem fit.

Any person or trade association can file information before the CCI for making an inquiry under the Competition Act. The CCI may also initiate an inquiry on its own motion.

Where a party is aggrieved by the order of the CCI, the party may resort to the following remedies:

- appeal to the Competition Appellate Authority Tribunal;
- appeal to the Supreme Court of India against any order or decision of the Competition Appellate Authority Tribunal.

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

India broadly follows the International Exhaustion Policy, that is, after the first sale of goods, the right holder of such goods exhausts all the rights over the goods internationally and such goods can be legally imported and distributed anywhere globally.

India's stand on parallel imports is not very clear or uniform, as there is certain legislation, such as the Patents Act 1970 and the Trade Marks Act 1999, with specific provisions that allow parallel imports into India, and then there is legislation, such as the Design Act 2000, which prohibits parallel imports, provided such designs are registered in India under the said Act.

The Customs Department of India in 2012 clarified that it shall allow free movement of parallel-imported goods in India, provided that the goods do not bear a false trademark or bear a false trade description as per the terms of the Trade Marks Act 1999.

Notwithstanding the acceptance of parallel imports under the Trade Marks Act 1999, the Act prohibits such imports if the goods are counterfeit or materially altered or impaired. Parties may also seek an injunction from the courts on the ground of infringement of trademarks.

Therefore, parallel import into India may be restricted by the suppliers under the contractual remedies available to them.

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

The supplier or distributor can advertise the products that they sell in the Indian market. Care should be taken that the contents of the advertisement should not be in violation of any laws in India. For example, the advertisement should be in compliance with the guidelines issued by the Advertising Standards Council of India. For certain products, such as cigarettes and other tobacco products, wine and spirits, and food products, the rules for advertising have been prescribed under law. Thus, the contents of advertisements for those products must be in compliance with the prescribed rules.

There is no legal prohibition on passing the cost of advertisement by the supplier to its distributors. The advertisement cost is a matter of agreement between the supplier and its distributors.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

The first step towards the protection of intellectual property rights is to register it in the country of its origin, and then register it in India. Also, protection can be obtained under any relevant international intellectual property convention or agreement to which India is a signatory.

There are certain intellectual properties, such as patents, that require mandatory registration for protection against any infringement. Trademarks are not mandatorily registrable. The protection of an unregistered trademark is also available under Indian law. However, a registered trademark enjoys better protection and infringement action is available for a registered trademark, unlike in the case of an unregistered trademark, where only a passing-off action can be initiated.

Similarly, copyright protection in India is provided automatically to the author of any original work. Registration is not mandatory. As India is a signatory to the Berne Convention for the Protection of Literary and Artistic Works, an author from any country that is a signatory of this convention is entitled to such rights as they allow to their own nationals, in addition to any rights granted under the convention. Notwithstanding this, it is advisable to register the copyright in India.

For patents, a separate registration must be done in India.

Apart from registration of registrable intellectual property, for those intellectual properties that are not registrable in India, such as trade secrets and know-how, strict non-disclosure and non-compete clauses can be incorporated in the distribution agreement. The distribution agreement can incorporate an indemnification clause against the distributor in case of any infringement of intellectual property rights by the distributor or any third party.

Further, the supplier can contractually limit the right of the distributor over the intellectual property owned by the supplier by granting a limited licence to use the intellectual property right over any product, on specific terms and conditions. It is advisable for the licence agreement to specify that transfer of any specific intellectual property right is without goodwill. Goodwill is a separate intangible asset.

Technology transfer agreements are common in India and they are legally enforceable, provided they are not anticompetitive or indulge in abuse of dominant position under the Competition Act.

26 What consumer protection laws are relevant to a supplier or distributor?

India has several legislative provisions pertaining to the rights of a consumer against a defective product. The main provision relevant to a supplier or a distributor is the Consumer Protection Act 1986. This statute provides for general product liability, protection from defective goods, and the redress available to the consumer. The other specific provisions in India pertaining to the quality, quantity and standards of the products that may be relevant to the supplier or distributor are, inter alia:

- the Indian Contract Act 1872;
- the Legal Metrology Act 2009 and the Legal Metrology (Packaged Commodities) Rules 2011;
- the Competition Act 2002;
- the Food Safety and Standards Act 2006;
- the Drugs and Cosmetics Act 1940;
- the Drugs and Magic Remedies (Objectionable Advertisements) Act 1954 and the Drugs and Magic Remedies (Objectionable Advertisements) Rules 1955;
- the Essential Commodities Act 1955;
- the Bureau of Indian Standards Act 1986; and
- the Standards of Weights and Measures Act 1976.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

There is no general legislation pertaining to recall of products distributed in the Indian market; however, there are certain specific legislative mandates for the recall of the distributed products. For instance, the Food Safety and Standards Authority of India has framed regulations, namely the Food Safety and Standards (Food Recall) Regulations 2017, which provide for the recall of food products that are considered unsafe. Further, the car industry is guided by the Voluntary Code on Vehicle Recall formulated by the Society of Indian Automobile Manufacturers, but that code is not legally binding and is voluntary in nature. The recalls done by the car industry are usually on account of safety issues, bad publicity, loss of reputation and such like. Further, the government has proposed the Motor Vehicle (Amendment) Bill 2017, wherein it is proposed that the central government would have the power to order a manufacturer to recall vehicles if they pose a risk to society.

In addition to the above, the courts have intervened on various occasions and have ordered the recall of products. In the event that the product quality does not match the standard prescribed under various applicable legislative measures, the authority concerned may also order the product to be recalled.

The parties can between themselves agree to the terms and conditions in the distribution agreement in the event of recall pertaining to cost absorption, and the roles and responsibilities of the supplier and distributor. In various legal precedents, the courts have emphasised that a manufacturer may be held liable for a manufacturing defect.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

Warranty is generally contractually provided by the seller to the buyer by way of express provisions in the agreement, and the extent

of warranty is also envisaged therein. However, the Sale of Goods Act 1930 imposes a duty whereby the sale of a product is subject to certain implied conditions pertaining to the quality of the goods. The said provision states that where the buyer, expressly or by implication, makes the seller aware of the purpose for which the goods are required, so as to show that the buyer has relied on the seller's skill or judgement, and the goods are to be used in the course of the seller's business to supply, there is an implied condition that the goods must be reasonably fit for such purpose, unless there is a contract for sale that there is no implied condition to the fitness of the product for any particular purpose.

Further, where goods of a particular description are purchased from a specialised seller who deals in goods of that description, there is an implied condition that they should be of merchantable quality, unless the buyer has examined the goods. In such a case, there shall be no implied condition with regard to defects that such an examination should have revealed.

Therefore, the sale agreement that is provided to the customer or to the end user can be formulated to limit the scope of warranties. However, the consumer courts, on various occasions, have extended the scope of warranty and have provided relief to the customer. In the absence of any warranty provided by the seller or any other conditions, the Indian courts have resorted to the imposition of the trade practice and have enforced a general warranty that may be applicable.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

There are no specific restrictions relating to the exchange of information between a supplier and its distributors about the customers and end users of their products. Data protection laws are not very evolved in India, unlike other jurisdictions, such as the United Kingdom. Aspects such as the purpose for collecting personal information, how this information will be used and so on are dealt with under different Indian laws. Specially, data in electronic form is protected, and regulations for the manner of its use have been provided under the Information Technology Act 2000 and the Information Technology (Reasonable Security Practices and Procedures and Sensitive Personal Data or Information) Rules 2011. Accordingly, if a corporation that deals with sensitive information is negligent in implementing and maintaining reasonable security practices to protect such sensitive information that results in wrongful loss or wrongful gain to any person, such a corporation may be liable to pay damages to the person affected thereby.

The courts in India have also taken the view that the right to privacy is a fundamental right, protected under the Constitution of India.

Therefore, in the absence of a comprehensive law relating to data protection, the provision for the sharing of data, ownership of data and so on should be expressly included in the agreement with the distributor. Covenants for confidentiality should also be incorporated in the agreement requiring the distributor to comply with the law.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

According to the Contract Act, there are no legal impediments in the event that a supplier wants to approve or reject the persons managing the distributor's business, if such a right is given to the supplier in the contract. Further, if provided under the contract, the supplier has a right to terminate the contract for the reason of being dissatisfied with the management of the distributors, and the same can be enforced. Caution must be taken when rejecting the management of the distributor, as the same distributor may claim unlawful termination and embroil the supplier in such a case. Therefore, an objective criterion for arriving at the conclusion of dissatisfaction or non-performance should be provided in the agreement in order to avoid any misinterpretation in case of a dispute. The contract for distribution must be carefully drafted to envisage the right to accept or reject the management of the distributor.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

Generally, agreements between suppliers and distributors are on a principal-to-principal basis. However, the terms of the agreement determine the nature of the relationship between the parties. In some cases, depending upon the level of supervision, control, approval process, organisational interference and such like, the relationship between the parties may not be considered as on a principal-to-principal basis, but the distributor may be treated as an agent or employee of the supplier. In the event that the courts reach a conclusion that a distributor or agent is an employee, then the same may result in implications under labour laws. Under Indian labour laws, employees are entitled to minimum wages, overtime, severance consequences, maternity benefits and other benefits.

The supplier can safeguard the potential risk of an agent or distributor being characterised as an employee of the supplier by carefully drafting the distribution agreement and incorporating covenants that safeguard the interests of the supplier.

32 Is the payment of commission to a commercial agent regulated?

Commission to be paid to a commercial agent is not regulated under Indian laws. The remuneration or commission to commercial agents is generally decided by the parties contractually considering the market practice, work attributable to the agent, and the time period for the commission of the work attributed after taking into account the transaction that the commercial agent would undertake. The (Indian) Ministry of Defence in the *Defence Procurement Manual* provides guidelines regarding commission paid to an agent in defence procurement.

33 What good faith and fair dealing requirements apply to distribution relationships?

Indian law does not provide any statutory provision wherein there is any requirement to perform a contract in good faith and fair dealings. Contracts are enforced strictly as per the terms of the agreement, and the courts have held that the intention of the parties should be construed on the basis of the terms of the contract only. However, the courts have emphasised the principle of negotiations between the parties in good faith (especially in insurance contracts, as the same is quintessential) but no rules have been laid down for contracts in general. The courts may give effect to the obligation to act in good faith in contracts. In trade practice, if the conduct of the parties undermines the just and fair standards of the industry, then enforceability of such clauses in the contract may be questioned on the basis of unreasonableness or contra proferentem rules.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

There is no provision under Indian law that provides for the registration of distribution agreements with a government agency or to obtain an approval from a government agency for the same. When dealing with intellectual property, a trademark licence agreement may be registered with the trademark office in India.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

Anti-bribery and corruption laws in India are applicable only in the instance of dealing with public officers or servants. The relationship between private suppliers and distributors would not come within the ambit of anti-bribery or anti-corruption laws in India. The said issues are to be dealt with on the basis of contractual covenants and policies framed by the suppliers and the distributors. It is fairly common in India to include bribery and corruption as a termination event of an agreement between suppliers and distributors.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

The Contract Act labels all contracts that restrain the exercise of lawful profession, trade or business of any kind by any party, as void. Through legal precedents, the courts have allowed reasonable restraints to be enforceable. Proper care must be taken to ensure that such contracts are drafted concisely in compliance with the provisions of the Contract Act, competition laws, consumer protection laws and other applicable laws.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

As a general rule, choice of law for governing the contract in the context of international commercial contracts is well recognised by the courts in India. The parties to the contract are free to agree on the applicable law of the contract between them, where the supplier is a foreign party and the distributor is an Indian party. If the supplier establishes its own entity in India and the distribution contract is signed between the Indian entity and the Indian distributor, then the governing law has to be the Indian law, as the contract, in such a case, would be between two Indian parties.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

Indian arbitration law enables the parties to choose any type of arbitral tribunal, whether ad hoc arbitration or institutional arbitration, to resolve their disputes. The place of arbitration can also be decided by the parties in the agreement. Parties can either agree for a foreign-seated arbitration, or a domestic arbitration to be conducted in India. An arbitral award passed either through a foreign-seated arbitration or a domestic arbitration is enforceable in India. However, at the time of choosing the place of arbitration outside India, care should be taken that the country is a signatory of the New York Convention or Geneva Convention for the enforcement of a foreign arbitral award. A foreign arbitral award passed in such a country would be easier to enforce in India as Indian arbitration law specifically provides for the enforcement of such a foreign award.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

Foreign businesses or suppliers are free to approach local courts (of competent jurisdiction) in India, unless arbitration is the consented form of dispute resolution or settlement. Where the dispute resolution mechanism is agreed as arbitration in the agreement by the parties, then the parties may approach the court in India only for limited purposes, such as interim measures and so on. That right is also dependent upon the agreement between the parties, since as per Indian arbitration law, the availability of the recourse of interim measures through an Indian court is a matter of agreement. Foreign businesses can expect fair treatment and the decisions of courts are free from bias. Since the procedures through Indian courts can be tedious, costly and time-consuming, the parties often agree on arbitration to resolve their disputes. However, a law relating to the specific Indian commercial courts has recently been enacted prescribing time-bound resolution of disputes through commercial courts. Therefore, the advantages and disadvantages of court procedure and arbitration should be evaluated in the context of the facts of each case before deciding the appropriate dispute resolution process.

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

An agreement to mediate or arbitrate disputes between the parties is well recognised under Indian law, and hence is enforceable in India. The choice of arbitral tribunal, place of arbitration, language of arbitration and such like is available to the parties. The parties may agree upon the manner of conducting the arbitration. It is common for foreign businesses to agree to arbitration for resolving disputes with their Indian business partners and distributors. The arbitration process provides for a certain liberty to the parties to resolve their disputes in the manner they want, especially with regard to timeline, number of arbitrators and so on, and arbitral awards are enforceable by Indian courts, subject to meeting the prescribed conditions under the arbitration laws for enforceability of the arbitral award.



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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

Generally, yes. There are two exceptions where a foreign supplier is prohibited from establishing a branch office or subsidiary in Japan: (i) where the country of the foreign supplier or the foreign supplier itself is subject to economic sanctions imposed by the Japanese government, it is necessary to obtain permission from the Minister of Finance to establish a branch office or subsidiary; and (ii) where the foreign supplier purchases shares in a Japanese corporation that conducts business in certain industries, such as broadcasting or airlines, there is a certain threshold that the foreign supplier's shareholding in such a Japanese company cannot exceed.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Generally, yes. See question 1 for restrictions on certain industries and those under the import and export regulations of Japan.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

A foreign supplier may use a branch office or subsidiary as a business entity in Japan. A partnership is not a common business entity for a foreign supplier.

While the most traditional and common vehicle for an importer owned by a foreign supplier has been the stock company (*Kabushiki Kaisha*, 'KK'), the limited liability company (*Godo Kaisha*, 'GK') is also gaining popularity as such a vehicle. Under the Japanese Companies Act, the registration procedure for the establishment of a KK in Japan requires the following:

- drafting of the articles of incorporation;
- obtaining the registration certificates and other necessary documentation for the incorporator; preparation of affidavits regarding the incorporator's profile and affidavits regarding the signatures of the incorporator's representatives;
- notarisation of the articles of incorporation by a Japanese notary public;
- payment of the full amount of capital;
- appointment of directors. The directors must investigate the legality of the company's formation; and
- application to the Legal Affairs Bureau for registration of establishment of the company. There is a registration tax of 0.7 per cent of the amount of capital (minimum ¥150,000).

In the case of the establishment of a GK, the appointment of representative members or managing members (or both) is required instead of the appointment of directors, however, the rest of the process is similar to the establishment of a KK.

The liability of GK members, like that of shareholders in a KK, is limited to the value of a member's investment in the GK. However, compared with a KK, the housekeeping matters (corporate governance structure, commercial registration, etc) for a GK are simpler, and incorporation fees (including registration fees) are less expensive.

Moreover, a GK can be a pass-through entity under a 'check-the-box regulation' for US tax purposes.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

Subject to those explained in question 1, there are generally no restrictions on non-resident individuals or foreign corporations from conducting business in Japan. However, if a foreign corporation continuously engages in business there, it at least needs to appoint a Japanese resident individual as its representative in Japan and have him or her registered with the competent legal affairs bureau.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

Generally, yes. See question 1.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

Non-resident individual

Income derived from business activities conducted by a non-resident individual will be taxable Japanese source income only, if the individual has a permanent establishment (PE) in Japan and the income is attributable to the PE.

Therefore, if a non-resident individual with no PE in Japan distributes his or her products directly to Japanese customers, the income derived from the distribution will not be taxable income for the purpose of the Japanese individual income tax.

Facilities used 'solely for the purpose of storage, display or delivery of goods' are excluded from the PE concept under most tax treaties between Japan and other countries.

However, in a case regarding a US-resident individual e-commerce distributor who distributes auto parts to Japanese customers and leases a small office and a warehouse in Japan for his or her business (*X v Japan*, *Gyosai Reishu* (Tokyo High Court, 28 January 2016)), a Japanese court held that the activities conducted through the office and warehouse were not 'preparatory or auxiliary' activities but established a PE in Japan under the Japan-US tax treaty. Subsequently, Japanese domestic tax law has clarified that warehouses and similar facilities are excluded from the PE concept only when they are used for 'preparatory or auxiliary' activities.

Foreign corporation

Direct distribution from overseas

Income derived from business activities conducted by a foreign corporation with no PE in Japan will not be taxable Japanese source income for the purpose of the Japanese corporation tax. A foreign corporation with no PE in Japan is not subject to local inhabitants' tax and local enterprise tax.

Branch office

If the foreign corporate distributor has a branch office in Japan, income derived from its business activities there and attributable to the branch office will be taxable Japanese source income. In such a case, the foreign corporation needs to submit an 'application form of foreign ordinary corporation' within two months of the date of establishment of the branch office, and file a tax return with the competent local tax office every year within two months of the date following the end of the foreign corporation's fiscal year.

Subsidiary

Where the distributor establishes a Japanese subsidiary to import products, the Japanese subsidiary's worldwide income (not only Japanese source income) will be taxable income for the purposes of the Japanese corporation tax, local inhabitants' tax and local enterprise tax.

On the other hand, a parent foreign supplier's income derived from selling products to its Japanese subsidiary shall not be subject to Japanese corporation tax.

If the transfer price of the products from the foreign supplier to its Japanese subsidiary is higher than the arm's-length price, the transfer price of the distribution transaction shall be deemed reduced to the arm's-length price for the Japanese corporation tax, and the Japanese subsidiary will be subject to additional Japanese corporation tax for the difference between the actual transfer price and the arm's-length price.

Distributions of retained earnings from a Japanese subsidiary to the parent foreign supplier are subject to Japanese withholding tax.

Local distributors and commercial agents**7 What distribution structures are available to a supplier?****Direct distribution**

Distribution by the foreign supplier through a subsidiary or branch (see questions 1 to 6).

Commercial agents

Agents in Japan for a foreign supplier can be categorised into a 'lawful agent' who is authorised by the foreign supplier to enter into sales agreements with customers in Japan, and (a pure 'commission agent' who is not authorised to do so, but is only authorised to act as an intermediary between the foreign supplier and those customers for the former's sale of goods to the latter.

In either of these cases, an agent in Japan does not purchase or acquire title to the products, but rather sells them on the foreign supplier's behalf and receives a commission. Generally, it is the foreign supplier (rather than the agent) who owns rights and owes duties under sales contracts with customers, unless the supplier authorises or delegates the agent to exercise or perform some of them on its behalf in the agency agreement.

Independent distributors

The foreign supplier may also contract with an independent distributor that buys products from the supplier, acquiring title to those products, and resells them at a profit (ie, a margin) to its own customers. This may be the most common structure for distribution in Japan.

Franchising

Typically, franchising equates to the use of independent distributors who are licensed to use the supplier's trademarks, either in their business name or in their products, are required to follow a prescribed marketing plan or method of operation, and pay a franchise fee to the supplier. Under Japanese law, there are no specific formal requirements to create a valid and binding franchise agreement. A franchise agreement is generally considered a combination of a licence agreement and a services agreement.

However, the franchisor must provide disclosure documents before entering into a franchise agreement, if the franchise business falls under the definition of a specified chain business under the Small and Medium-sized Retail Business Promotion Act. As this Act is designed to protect small and medium-sized retail businesses, the disclosure obligations will not be imposed if the majority of the franchisees are large and sophisticated.

Joint ventures

A joint venture can be established by a foreign supplier with its distribution partner in Japan, whether the partner is an agent, distributor or franchisee, by having the local distribution entity owned in part by the supplier, directly or through a subsidiary, or through another form of sharing of profits and expenses. An ownership interest can provide greater control through ownership rights and representation on a board of directors or management committee.

Licensing of manufacturing rights

A foreign supplier may license a manufacturer in Japan to use its intellectual property, such as patent, copyright, trademark or trade secrets, to manufacture its products locally and have them sold in Japan. Care must be taken by the licensor to maintain quality control over the finished products and the licensee's use of the intellectual property. Failure to do so can not only put the brand equity at risk, but can also risk the loss of trademark protection.

Private label (original equipment manufacturer)

Distribution of products under a private label amounts to a reverse licensing arrangement, where a distributor or retailer in Japan distributes the foreign supplier's products under the Japanese distribution partner's own trademark. In essence, the supplier gives up its own brand name in exchange for the distribution strength of its partner in Japan, with the supplier reaping no enhanced brand value. Control over sales, distribution, marketing and advertising are in the hands of the local brand owner, resulting in negligible distribution costs to the supplier, and virtually no control in the hands of the supplier, save for sales and performance benchmarks in the contract, with benefits to the supplier limited to its profits on sales of the products.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

Agency and distribution agreements in Japan, as contracts, are generally governed by the Civil Code. There are no special laws governing agents and distributors.

However, as you will see below, in reviewing the legality of some provisions in an agency or distribution agreement, the Antimonopoly Act and the regulations promulgated thereunder (collectively, the AM Act) (and the 'Guidelines Concerning Distribution Systems and Business Practices' issued by the Japanese Fair Trade Commission – the Guidelines) especially should be taken into account. The government agency that is primarily in charge of enforcement of the AM Act is the Japanese Fair Trade Commission (JFTC). Some industries have also adopted their commercial associations' voluntary rules concerning the above national laws and regulations.

In addition, transactions involving the movement of goods, services or capital between Japan and foreign countries concerning an international agency or distribution agreement are subject to the Foreign Exchange and Foreign Trade Act and the regulations promulgated thereunder (collectively, the FEFT Act).

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

Japanese courts, through past decisions, have established a doctrine for protecting a party to a 'continuous transaction agreement' from illegal or unlawful termination thereof by the other party (the Continuous Transaction Agreement Doctrine). An agency, distribution or franchise agreement can fall within the meaning of such a 'continuous transaction agreement' if it has continued for a certain period of time. Under the Continuous Transaction Agreement Doctrine, if a commercial agreement has lasted for a long time, such an agreement may be unilaterally terminated by one of the parties thereto only if there is either a 'justifiable reason' for the termination, or the terminating party gives reasonable notice to the other party.

The application of the Continuous Transaction Agreement Doctrine by Japanese courts is generally made, taking into account numerous factors surrounding each specific case. Such factors include the length, term and type of the agreement in question, the nature of the 'justifiable reason' asserted by the terminating party, the degree and reasonableness of the terminated party's reliance on the continuation of the agreement, and the difference in bargaining power between the parties involved. Courts also consider the length of prior notice (if any), and the amount of compensation (if offered).

The Continuous Transaction Agreement Doctrine applies regardless of whether the agreement at issue has a specific term, or whether it is terminated at the end of or in the middle of its term. However, courts generally review the legality of a termination of the agreement in the middle of its term with more scrutiny, compared to non-renewal thereof at the end of its term.

If the attempted termination of a continuous transaction agreement is deemed illegal and unlawful due to application of the Continuous Transaction Agreement Doctrine, the terminated party may (i) seek the court's declaration that the agreement remain in force, (ii) demand the terminating party's performance of the agreement, (iii) seek an injunction against the terminating party's breach of the agreement or (iv) claim for damages incurred by it due to the terminating party's breach or illegal termination of the agreement.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

As explained in question 9, if a party's attempted termination of an agency, distribution or franchise agreement (especially when it is attempted without cause) is deemed illegal due to application of the Continuous Transaction Agreement Doctrine, the terminating party may be required to compensate for damages incurred by the terminated party due to the illegal termination.

In such cases in the past, Japanese courts determined that the terminating party should pay, as compensation for such damages, an amount equivalent to the gross (or net) profit which the terminated party could earn for the remainder of the term of the agreement or for a period from six months to two years.

Furthermore, if the termination of a continuous transaction agreement causes other 'special loss', and if such special loss is reasonably foreseeable at the time of the termination, the terminating party would be liable for such special loss (eg, costs related to those employees of the terminated party who were exclusively engaged in the business under the continuous transaction agreement in question).

If, due to the termination of the agreement, those employees were dismissed compelling the terminated party to incur costs, such as the payment of severance in accordance with the relevant Japanese practices, and if such dismissal of the employees was reasonably foreseeable by the terminating party when it terminated the agreement, the court could determine that such loss would also be required to be compensated.

On the other hand, if a termination of a continuous transaction agreement is considered permissible despite the possible application of the Continuous Transaction Agreement Doctrine, the terminating party will in principle not be required to compensate the terminated party.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

Under Japanese law, contract provisions prohibiting the transfer of distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor's or agent's business to a third party, will generally be enforceable subject to the following.

- The supplier shall not be able to assert, as against a bona fide third party, that a transfer made by the distributor or agent violating the applicable contractual provision be void.
- The contractual provision in a distribution agreement prohibiting the distributor's assignment of the agreement may not work, as intended, to limit such assignment in the case of a corporate merger (where Corporation A and Corporation B merge into and form one Corporation A + B) or a corporate split (where Corporation A splits

into two corporations: Corporation A and Corporation B). This is because the agreement will, by operation of law, be automatically assigned to the surviving corporation (in the case of a corporate merger) or the corporation that is to assume the agreement according to the relevant corporate split agreement (in the case of a corporate split).

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

Under Japanese law, there is generally no limitation on the extent to which confidentiality provisions in distribution agreements will be enforced.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

During the term of an exclusive distribution agreement, restrictions on a distributor's handling of competing products are not illegal from the viewpoint of antitrust regulations, unless such restrictions prohibit the distributor from handling competing products it had been dealing with before the conclusion of the agreement. Where such restrictions prohibit the distributor from handling even competing products it had been dealing with before the conclusion of the agreement, the legality of such restrictions will be examined by the JFTC according to the case, taking various factors into consideration, to determine whether the restrictions have the effect of excluding competitors from the market.

Regarding the non-exclusive distribution agreement, restrictions on handling competing products during the term of the agreement are examined by the JFTC from the viewpoint of whether such restrictions are imposed by an 'influential manufacturer in a market' (defined as a manufacturer which has a market share of 10 per cent or more, or is ranked in the top three in the market) and whether they may result in making it difficult for new entrants or competitors to easily secure alternative distribution channels. If the JFTC finds such effect in the restrictions, they will be determined illegal as an unfair trade practice.

A prohibition on handling competing products after the term of a distribution agreement has expired is generally considered illegal, except where (i) that distribution agreement is exclusive, (ii) the term of such extended prohibition is less than two years after the expiry of the agreement, and (iii) there is a reasonable rationale for the prohibition, such as the necessity to protect confidential trade secrets.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

Under the AM Act, so far as distribution of products in the Japanese market is concerned, a supplier in principle cannot control the prices at which its distribution partner resells its products, as such resale price maintenance is illegal as an unfair trade practice.

However, under the Guidelines, the supplier's provision of its instructions regarding resale price to the distributor will not be deemed illegal in cases where the distributor, as a direct purchaser from a supplier, only functions as a commission agent for the supplier so that the supplier is substantially deemed to be selling its products to the ultimate purchasers.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

Under the AM Act (and the Guidelines), in cases where a supplier's 'suggested' retail price or quotation is indicated to its distributor as a mere reference price, it would not be a problem. However, if the supplier substantially seeks to restrict the resale price of the distributor by causing it to maintain the reference price by some means (eg, by announcing that it will not deal with distributors who do not follow its pricing policy), it will in principle be illegal.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

Under Japanese law, the distribution contract may, generally, specify that the supplier's price to the distributor will be no higher than its lowest price to other customers.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

Under the AM Act, discriminatory pricing defined as 'unjustly supplying or accepting a commodity or service at prices which discriminate between regions or between the other parties' is prohibited as an unfair trade practice. Accordingly, if there is a justifiable reason for a difference in prices, it would not be deemed illegal. However, it is generally said that in cases such as the following, a difference in prices is likely deemed to be illegal in view of its anticompetitive effect:

- where the seller sells its products at lower prices only in a territory in which the seller is competing with another seller of the same or similar products, in order to exclude the competitor from the market; or
- where the seller sells its products at lower prices only to customers of its competitor, in order to exclude the competitor from the market.

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

Under the AM Act and the regulations promulgated thereunder (and the Guidelines), it is not illegal for a supplier to adopt the system for designating a geographic area of its distributor's sales responsibility or for the location of its business premises for the purpose of developing an effective network for sales or securing a system for good after-sales services, unless the restriction falls under an 'exclusive territory' (meaning a restriction on the distributor from actively selling outside the designated area) or a 'restriction on sales to outside customers' (meaning a restriction on the distributor from even passively selling to customers outside the designated area upon their request).

However, in the case where a supplier requires its exclusive distributor not to actively market the product covered by the distribution contract in areas outside the territory for which the exclusive distributor is granted the exclusive distributorship for the product, it would in principle present no problem under the AM Act.

On the other hand, even in the case of an exclusive distributorship agreement under which a supplier grants its distributor the 'exclusive' right to sell a product in a territory, it is generally possible for the parties to agree that the supplier will reserve the right to sell the product to certain customers in the territory.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

Under the AM Act, a supplier's restriction or prohibition on e-commerce sales by its distributor is deemed to be a kind of restriction on the distributor's sales methods. Accordingly, whether such a restriction or prohibition is illegal will be determined in accordance with what we describe in question 22.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

Under the AM Act (and the Guidelines), it is generally not illegal for a supplier, as a single firm, to refuse to deal with particular customers in view of the general freedom it should have in choosing which customers it will do business with, unless such a refusal to deal is made in order to secure the effectiveness of its illegal conduct under the AM Act (eg, resale price maintenance) or to achieve unjust purposes thereunder (eg, exclusion of its competitors from a market).

On the other hand, if a supplier restricts its distributor's ability to deal with certain customers, it will be illegal as an unfair trade practice

if the price level of the product covered by the restriction is likely to be maintained thereby.

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

A distribution or agency agreement per se will not be deemed a reportable transaction under Japanese merger control rules or require advance clearance by the competition authority (ie, the JFTC).

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

In the case where a supplier restricts its distributor's sales methods for the product covered by the distribution contract or causes the distributor to restrict its sub-distributors' sales methods, it may pose a problem under the AM Act unless there is a good reason for the purpose of ensuring proper sales of the product (eg, assurance of safety of the product, preservation of its qualities or maintenance of credibility of its trademark) and the same restrictions are applied to its other distributors on equal terms.

Especially in cases where restrictions on the distributor's sales methods are used as a means of restricting sales price, handling of competing products or sales territory or customers, their legality is to be judged from the perspective of whether they constitute a resale price restriction, a dealing on exclusive terms or a dealing on restrictive terms that may be deemed illegal under the AM Act.

The agency in charge of enforcing the regulations under the AM Act is primarily the JFTC. When it finds that there is a violation of those regulations, it can (i) issue a warning, (ii) issue a caution, (iii) issue a cease-and-desist order, (iv) order the payment of a surcharge, or (v) seek an injunction at the Tokyo High Court.

Any (private) person who suffers damages caused by an act violating the AM Act can claim for damages based on the general theory of tort under the Civil Code or under a special provision in the AM Act. Further, under the AM Act, a person whose interests are infringed or likely to be infringed by an act constituting an unfair trade practice and who is thereby suffering or likely to suffer serious damages, is entitled to demand the suspension or prevention of such infringements from an entrepreneur or a trade association that infringes or is likely to infringe such interests.

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

Under Japanese law, there is no way for a distributor or agent to legally prevent parallel or grey market imports into its territory of the supplier's products, except:

- where products being sold as parallel or grey market import goods are not genuine products but are counterfeit products;
- when it is necessary for maintaining the credibility of a trademark in the case where consumers may have been led to understand that parallel or grey market import goods with a different specification or quality are identical to the product handled by a distributor or agent due to misrepresentation of origin or other reasons; or
- when it is necessary for maintaining credibility of a trademark in the case where credibility of the product handled by a distributor or agent may be damaged due to threats to consumers' health or safety caused by deterioration of the parallel or grey market import goods.

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

Under the AM Act (and the Guidelines), where a distributor in a dominant bargaining position, for its own convenience, causes the supplier

to pay monetary contributions or inflict other financial burdens for the cost of advertising, it is most likely to unjustly favour the distributor and present a problem as an abuse of dominant bargaining position.

On the other hand, a supplier may generally pass all or part of its cost of advertising on to its distribution partner or share in its cost of advertising, by agreement to that effect with its distribution partner.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

Trademarks

Trademarks are generally protected only upon registrations through the Japan Patent Office (JPO). Japanese trademark registration can also be obtained under the Madrid Protocol, if the supplier's home country is a signatory to the treaty.

Only the owner of a trademark may obtain a Japanese registration. Accordingly, in general, the supplier, rather than the local distributor, will be the applicant. Contracts typically forbid the distributor from registering the trademark, in order to protect the supplier from infringement by its distribution partner. Some contracts allow the distribution partner to register itself as a licensee of the trademarks in Japan, but it is risky for the supplier. Especially so if the distribution partner is registered as the exclusive licensee of the trademarks in Japan, when even the supplier cannot use its own trademarks there unless the registration of the distribution partner as such is abolished, resulting in the greater bargaining power of the distribution partner when the supplier attempts to terminate the distribution agreement.

Patents and utility models

Patents and utility models are generally protected upon registrations through the JPO. Japanese patent and utility model registration can also be obtained under the Patent Cooperation Treaty, if the supplier's home country is a signatory to the treaty.

The distribution partner's unauthorised sale of products protected by a patent or utility model is usually regulated by contract, but can also be remedied through an infringement suit.

Registered designs

Under Japanese law, designs can also be protected upon registrations through the JPO.

The distribution partner's unauthorised sale of products protected by a registered design is usually regulated by contract, but can also be remedied through an infringement suit.

Copyright

The copyright in a copyrightable work is protected without registration from the moment the work is created. While the copyright as an economic right is transferable (and the transfer can be asserted against a third party upon registration), the moral right in a copyrightable work is not transferable.

The distribution partner's unauthorised use of materials protected by copyright is usually regulated by contract, but can also be remedied through an infringement suit.

Trade secrets and know-how

The supplier's trade secrets and know-how are generally protected in accordance with confidentiality provisions in the distribution agreement.

In addition, the Unfair Competition Prevention Act (UCPA) provides for some 'act of unfair competition' categories regarding misuse or improper disclosure of trade secrets. A trade secret is protected under the UCPA if it consists of technical or business information that is useful for commercial activities, and it is kept secret and not publicly known. Remedies for such an act of unfair competition are an injunction and compensation for damages.

Technology-transfer agreements

Technology-transfer agreements are not commonly used to structure the relationships between commercial suppliers and their distribution partners, where a licence agreement is more common.

26 What consumer protection laws are relevant to a supplier or distributor?

Under Japanese law, so long as neither the supplier nor its distributor is an individual, no consumer protection law will apply to regulate the relationship between them.

However, inasmuch as the products to be supplied by the supplier to its distributor for distribution in Japan are sold to general consumers, consumer protection laws may apply to the sales or the products sold. Such laws include the Product Liability Act, the Consumer Product Safety Act and the Consumer Contract Act, in addition to the statutory warranty and other relevant provisions in the Civil Code. The Act Against Unjustifiable Premiums and Misleading Representations may also apply to regulate the contents of the supplier's and distributor's advertisements.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

Under the Consumer Product Safety Act, in cases where 'serious product accidents' have occurred due to a defect in the consumer products or where serious danger has occurred to the lives or safety of general consumers or the occurrence of such danger is considered to be imminent, when the competent minister finds it particularly necessary to prevent the occurrence of and increase in this danger, to the extent necessary the minister may generally order the person engaging in the manufacture or import of the consumer products to recall the products in question and otherwise take measures necessary to prevent the occurrence of and increase in serious danger to the lives or safety of general consumers due to the products. (In addition, a 'voluntary' recall may be made by the manufacturer or importer.)

It is prudent to define in the distribution contract the parties' respective responsibilities in the event of a recall, including who may decide to initiate a recall, how it will be implemented, and who will pay the costs, including credit that customers may require for recalled products. Without such defining provisions in the contract, it is likely under Japanese law that the supplier (rather than the distributor) will eventually be responsible for all of the costs reasonably required to be incurred for a recall.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

Under Japanese law, so long as neither the supplier nor its distributor is an individual, any limitations on the supplier's warranties to be provided to its distribution partner will generally be valid and effective, except that the supplier cannot deny its liability for a loss of a person's life or his or her bodily injury or its liability for damages caused by its intentional act, for reasons of Japanese public policy.

However, inasmuch as the products to be supplied by the supplier to its distributor for distribution in Japan are sold to general consumers, certain provisions in the sales agreements limiting the seller's warranties provided to general consumers may be deemed void under the applicable provisions in the Consumer Contract Act.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

Companies collecting personal information regarding individual customers must generally describe, as specifically as possible, the purposes of their use of personal information to be collected from them; and they cannot exceed the scope of such purposes of use or transfer the personal information to any third party without the prior consent of the relevant individual customers, except in certain prescribed circumstances. Particularly in the case where a Japanese company intends to transfer such personal information to a third party located in a country other than Japan, prescribed circumstances available as exceptions to the general rule (requiring the prior consent of the relevant individual customers) are more limited than in the case where such a third party transferee is located in Japan. In addition, when a Japanese company

discloses such personal information to, or receives it from, a third party, whether located in Japan or in a country other than Japan, the Japanese company must generally make a record of certain items designated by statute (eg, the name of the third party) that are relevant to such disclosure or receipt of the personal information and keep such record for a prescribed period of one to three years, depending upon the type of record, except in certain prescribed circumstances. Within those constraints, and subject to any specifically regulated areas (and further subject to any applicable regulations of a foreign country), the distribution partner may generally exchange its customer information with the supplier.

Parties should clearly define in their distribution contract who will own the customer information that will be collected, who will have access to it, and the applicable confidentiality obligations to be respectively owed by them. In the absence of such a definition, customer information is likely to belong to the party that collected it and any transfer thereof by that party to the other party will be subject to applicable data protection or privacy regulations.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

Under the general principle of freedom of contract that is recognised under Japanese law, the parties may generally provide as they wish with respect to the supplier's control over those who manage the distributor. Accordingly, the distribution contract can grant authority to a supplier to approve or reject the individuals who manage the distribution partner's business, or to terminate the contract if not satisfied with the management.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

Under Japanese law, a distributor cannot be treated as an employee of the supplier.

On the other hand, an agent, especially when it is an individual or a single-employee company or sole proprietorship, might be deemed an employee of the supplier. The principal test for distinguishing an independent contractor from an employee is whether the supplier allows the agent their own discretion in performing their services rather than having them perform their services under the complete direction and supervision of the supplier. Misclassification may result in substantial employment and tax liabilities for the supplier, including retroactive pay and benefits. Employees are generally entitled, among other benefits, to minimum wage and overtime compensation, unemployment benefits, and workers' compensation.

The supplier should include a provision for indemnification in its contract with the distribution partner, in order to protect itself against any responsibility for potential violations of labour and employment laws by its distribution partner.

32 Is the payment of commission to a commercial agent regulated?

Under Japanese law, there are generally no regulations on the payment of commission to a commercial agent.

33 What good faith and fair dealing requirements apply to distribution relationships?

There is a general principle requiring good faith and fair dealing from parties to a contract when they perform it. This general principle may apply to the parties to a distribution contract. In particular, the Continuous Transaction Agreement Doctrine referred to in question 9 can be interpreted as being based on this general principle of law.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

There is no legal requirement for the registration of a distribution agreement with any Japanese governmental agency.

On the other hand, under the FEFT Act, there is a filing requirement for an agreement under which industrial property or know-how is licensed by a foreign licensor to a Japanese licensee. However, this requirement applies only when the licensed industrial property or know-how relates to any of the following five designated categories: (i) aircraft; (ii) weapons; (iii) manufacture of explosives; (iv) nuclear power; or (v) development in outer space. If the licensed industrial property or know-how falls under any of the above-designated categories, a prior notification on conclusion of the licence agreement must generally be filed with the competent ministers through the Bank of Japan unless the amount of consideration for the licence is ¥100 million or less (in which case, an ex post facto report will suffice). Accordingly, a foreign supplier's grant to its distribution partner of the right to use a trademark, made with regard to a distribution right for Japan, will generally not be subject to the filing requirement as we cannot think of a situation where such a trademark falls under any of the above-designated categories.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

Japanese law encompasses certain anti-bribery and anti-corruption regulations. Most notable for an international distribution relationship are the provisions under the UCPA that address bribery of foreign public officials. The UCPA applies to (i) an individual of any nationality, if all or part of the violating act is committed in Japan, and (ii) a Japanese national who offers a bribe to any foreign official regardless of where the conduct occurs. The UCPA may also apply to an entity whose representative, agent or employee has engaged in the above types of conduct.

Of course, a foreign supplier should be cautious about any risks related to any possible misconduct by its distribution partner in Japan, to which not only the anti-bribery or anti-corruption law of Japan, but also that of a foreign country, may apply.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

Except for the specific industry or franchise regulations and the restrictions under the AM Act (as discussed above), the parties are generally free to structure their distribution relationship as they desire.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

Japanese courts will generally recognise the parties' contractual choice of law to govern a distribution contract.

However, when the distribution contract is concluded for the purpose of distribution in the Japanese market, there are certain mandatory local regulations that apply to a distribution agreement, despite the parties' contractual choice of a foreign law. Such mandatory local regulations include those under the AM Act and the Continuous Transaction Agreement Doctrine established by judicial precedents that may apply to an attempted termination of the distribution contract (see questions 9 and 10). In this connection, the Guidelines include a section entitled 'Major Restrictive Provisions in Exclusive Distributorship Contracts'.

In addition, it should be noted that since Japan is a signatory to the United Nations Convention on Contracts for the International Sale of Goods (1980), the provisions of an international distribution contract to be concluded by a Japanese party may be superseded by those of the Convention, unless the contract contains the parties' agreement to exclude the application of the Convention.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

Japanese courts will generally recognise the parties' contractual choice of courts or arbitration tribunals, whether inside or outside Japan, to resolve contractual disputes.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

When a dispute arising under an international distribution agreement is brought before a Japanese court, it will be presided over by a regular court so long as the court has jurisdiction over the dispute, and the legal action will proceed in accordance with the Code of Civil Procedures and the regulations promulgated thereunder. In such a legal action, a Japanese court may issue a decision ordering the losing party to pay monetary compensation for damages incurred by the winning party or declaring restoration of the contract based on the grounds that attempted termination thereof should be deemed void.

Even foreign businesses are not restricted in their ability to make use of a Japanese court and the procedures for a legal action before such a court, so long as it has jurisdiction over the relevant dispute; and they can generally expect fair treatment by a Japanese court.

Under Japanese civil procedure law, no extensive 'discovery' system which allows one party to request that another party disclose and produce documents and other materials outside the proceedings before the court, is in place for a legal action before a Japanese court. What is available instead is the more limited scope of a court order to produce documents and other materials that may be issued upon a party's request made through the proceedings before the court. The system of 'deposition' to be made by a party outside the court is also not in place for a legal action in Japan. Testimony from an adverse party will only be given in the trial before the court, after the court admits a party's request for such a testimony.

The advantages to a foreign business of resolving a dispute in Japan in a legal action before a court may include (i) less likelihood that a Japanese court would deny its jurisdiction over the legal action brought against a Japanese party; (ii) no need to prove Japanese law when it is the law governing the dispute; and (iii) the ease in enforcing the Japanese court's judgment to be rendered in favour of the foreign business by a court's order of attachment to an asset of the Japanese party located in Japan. On the other hand, the disadvantages may include (i) costs associated with the action (including translation costs, as the legal proceedings and submission of a document therein, in principle, need to be carried out or made in Japanese), and (ii) the foreign business's unfamiliarity with the Japanese system.

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

Under Japanese law, the parties' agreement to arbitrate disputes arising under a contract will generally be effective and enforceable. There is no particular limitation on the terms of their agreement to arbitrate, so long as they are consistent with the arbitration rules (such as those established by an arbitration association) chosen by them to apply to an arbitration for such disputes.

The advantages to a foreign business of resolving a dispute with its business partner in Japan by arbitration may include (i) the principle that once a final award is rendered by the arbitrator(s), it will become final and binding without the need to go through any appellate proceedings, resulting in less time until the dispute is resolved; (ii) the principle that the arbitration proceedings will not need to be carried out in a manner open to the public, which may be more suitable depending upon the subject of the dispute and the need to avoid the dispute negatively affecting the party or parties in public; (iii) the flexibility in defining some practical rules for arbitration; and (iv) the relative ease in enforcing in Japan an arbitration award to be rendered in favour of the foreign business, due to the fact that Japan is a signatory to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958) (the New York Convention). On the other hand, the disadvantages may include (i) costs associated with arbitration (including fees for arbitrator(s) that may be substantial), and (ii) potential difficulty in finding good arbitrator(s) suitable for and capable of resolving the dispute, using the language selected by the parties for the arbitration.

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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

A foreign supplier can establish its own entity in Puerto Rico to import and distribute its products as long as it has not previously granted rights to local distributors that are inconsistent with the establishment of the supplier's own entity.

For example, the Puerto Rico Dealers' Contracts Act (Law No. 75 of 24 June 1964), 10 PR Laws Ann sections 278 et seq (Law 75) regulates the relationship between a supplier and its distributor, and establishes a rebuttable presumption of impairment in cases when the supplier establishes facilities in Puerto Rico for the direct distribution of merchandise, the distribution of which was previously granted to the distributor. This is particularly applicable to situations where the distributor has exclusive distribution rights.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Law 75 does not prevent or limit a foreign supplier from acquiring partial ownership in a local company that is the importer of its products. Depending on the amount of equity and control acquired by the supplier in the local company, however, practical and legal issues regarding governance of the entity, its operations and the distribution relationship between the local company and the supplier may have to be considered in light of Law 75.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

Various forms of business entities are available, but the forms most used are corporations and limited liability companies (LLCs).

Puerto Rican corporations and LLCs are formed by filing articles of incorporation or organisation with the Department of State. The entity must maintain at all times a local office and a resident agent for service of process.

Foreign corporations and foreign LLCs may also be registered by filing an authorisation to do business with the Department of State.

Registrations are made online and they require a US\$150 government filing fee for corporations and US\$250 for LLCs. To maintain their registrations, corporations must file corporate annual reports along with a US\$150 filing fee. These reports must include a balance sheet. LLCs only have to file a US\$150 annual filing fee; no report is required. These fees change from time to time.

Corporations and LLCs are governed by the Puerto Rico General Corporations Act of 2009 (Act No. 164 of 16 December 2009), as amended, which has been drafted in its majority to mirror Delaware's statutes.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

There are no specific restrictions as to foreign investment and foreign ownership of domestic entities. Generally, foreign businesses are subject to the same requirements as Puerto Rican entities. Since federal laws extend to Puerto Rico, federal controls on foreign investments are

applicable. In cases involving foreign (non-US) individuals doing business and residing in Puerto Rico, immigration laws will apply.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

See question 2.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

Income taxes

Companies organised in Puerto Rico are subject to Puerto Rican income tax on their worldwide income. Foreign companies engaged in trade or business in Puerto Rico are taxable only on the income generated from sources within Puerto Rico and certain types of income effectively connected with operations in Puerto Rico except for services rendered to US and Puerto Rican government entities that are Puerto Rican sourced income independent of where ordered. Partnerships and limited liability companies electing to be taxed as partnerships are not subject to tax, but net income is assigned to the partner or member who is responsible for payment of the applicable income taxes. Puerto Rican companies that are subject to taxation outside Puerto Rico may claim a tax credit for income taxes paid to a foreign jurisdiction, subject to certain limitations. Similarly, foreign companies subject to tax in Puerto Rico may claim a credit for the taxes paid to Puerto Rico depending on the law of the jurisdiction of their organisation.

The corporate income tax rate ranges from 20 to 39 per cent of the net income of the entity. The alternative minimum tax (AMT) is intended to prevent taxpayers from reducing their income tax liability by benefiting from substantial tax preferences. The AMT is the amount by which the tentative alternative minimum taxable net income for the taxable year exceeds the regular tax for the taxable year.

Generally, dividends paid by Puerto Rican companies, or by certain foreign companies engaged in trade or business in Puerto Rico, to residents and non-resident persons are subject to a 15 per cent withholding tax. A dividend received deduction of 85 per cent is allowed on dividends received by a company engaged in trade or business in Puerto Rico from a domestic (Puerto Rican) corporation (100 per cent in the case of a controlled Puerto Rican company).

Net long-term capital gains upon the exchange or sale of investment and business assets held for more than one year by a company are subject to a 20 per cent tax (15 per cent for individuals). Inventory is not considered a capital asset. Capital losses are allowed up to 80 per cent of the net capital gain generated in the taxable year. Unused capital losses can be carried forward until exhausted, subject to the 80 per cent limitation.

The determination of net income is made under generally accepted US accounting principles. The net income of the company is adjusted to reflect the tax treatment of items of income and deductions. In general, financial statements audited by a certified public accountant authorised to practise in Puerto Rico must be attached to the company's income tax return if the volume of business of the company reaches US\$3 million during the taxable year. Certain supplementary information must also be included.

Net operating losses are carried forward up to 10 years and are allowed up to 80 per cent (90 per cent for 2019) of net taxable income. Puerto Rican source income derived by foreign companies not engaged in trade or business in Puerto Rico is subject to a 29 per cent withholding tax. This tax also applies to interest paid from sources in Puerto Rico to a related foreign company not engaged in business in Puerto Rico (interest paid to unrelated persons is not subject to withholding taxes).

Sales and use tax

Puerto Rico imposes a sales and use tax (SUT) upon the introduction, sale, consumption or use of a taxable item (eg, tangible personal property, taxable services, etc). The SUT rates are 10.5 per cent (4 per cent SUT applies on certain services) for the state and 1 per cent for the municipalities.

The SUT applies to services rendered by a non-resident person or company to a company engaged in trade or business as well as to management fees and inter-company transactions within a controlled group. A company cannot commence operations in Puerto Rico unless it is registered as a merchant for SUT purposes. The declaration and payment of the SUT must be made online through the portal established by the tax agency.

Other important taxes

Municipal licence tax (gross volume of business tax) is 1.5 per cent for financial businesses and 0.5 per cent for others and must be declared and paid to each municipality in which the business maintains a commercial location.

Property taxes range from 5.80 to 10.33 per cent and real property tax ranges from 8.03 to 12.33 per cent depending on the municipality in which the property is located. These rates are for fiscal year 2018–2019 (rates for fiscal year 2019–2020 were not available at the time of writing).

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

The distribution structures available to a supplier doing business in Puerto Rico include direct distribution by the supplier or an affiliate, independent distribution, sales representatives, franchising, brokers, private labelling, trademark licensing and joint ventures. The choice of the structure will depend on the nature of the supplier's business and the manner in which it wishes to develop, operate and control its business in the Puerto Rican market. In addition, the determination of which law will apply to the distribution structure may influence which structure is used. For example, distribution and franchise relationships may be covered by Law 75, while sales representatives and maybe even some brokers and agents could be covered by the Sales Representative Act (Law No. 21 of 5 December 1990), 10 PR Laws Ann sections 279 et seq (Law 21). Law 21 protects sales representatives in a manner similar to the protection extended to distributors under Law 75.

Both Law 75 and Law 21 are highly protectionist statutes that therefore require careful analysis, on a case-by-case basis, prior to setting up distributor or sales representative relationships.

There is no specific statute in Puerto Rico governing or regulating the creation of, operation or investment in franchises as such, and those aspects of doing business with franchises would generally be subject to US laws and covered by the Federal Trade Commission rule, because Puerto Rico is part of the United States. The relationship between a franchisor and its franchisees, of course, has many of the characteristics of a plain, non-franchise labelled distribution relationship and as such may be covered under Law 75. Moreover, Law 75 specifically lists distribution by franchise as covered by the statute.

Other distribution structures, such as those with brokers, independent label sellers, joint ventures with the distributor or sales representatives and contracts for logistics and warehousing services may or may not be covered by the two main statutes depending on the nature and specifics of the relationship, and have to be analysed case by case.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

Law 75 regulates the relationship between a supplier and its distributor that is actively promoting the supplier's product in Puerto Rico. Law 21 regulates the relationship between the supplier's agent acting as a sales representative and the supplier. Both of these laws regulate relationships within the chain of sale or distribution. Any matter not specifically covered by the specialised statutes will be supplemented by the Puerto Rico Commerce Code (10 LPRA sections 1001 et seq) and the Puerto Rico Civil Code (31 LPRA sections 1 et seq).

There is no government agency entrusted with particularly enforcing these two statutes. Judicial enforcement is the most common method of invoking the rights afforded by these two specialised laws. Arbitration is another common method for resolution of disputes arising under the two statutes or under more general principles of law covering the distribution or sales representation relationship.

Both distributors and sales representatives are bound by regulations under the Department of Consumer Affairs (DACO), which regulates truth in advertising, promotional campaigns and contests and related matters. While this agency and its regulations may not typically govern the formation, existence or termination of the relationship, they do frequently affect how distribution and sales representation is done and therefore 'regulate the relationship' to a certain extent.

There are no formal self-regulatory constraints that would officially affect the distribution or sales representation relationship.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

Even if allowed by contract, Law 75 and Law 21 prohibit either the termination of a distribution relationship during its contracted term or the refusal to renew it at expiry, unless there is just cause or the distributor or sales agent is compensated for the termination or refusal to renew, assuming it is entitled to compensation.

Under either Law 75 or Law 21, there is no specific list of acts or events that constitute statutory just cause allowing termination of a distribution or sales representative contract. Both laws, however, define the concept in general form, as follows: (i) the breach by the distributor or sales representative of its essential obligations under the distribution or sales representation agreement; or (ii) any act or omission of the distributor or sales representative that adversely and substantially affects the interests of the principal or grantor (supplier) in the development of the market or the sale of merchandise or services.

Case law has identified examples of situations that will more likely than not meet the general just cause criteria of the statute, such as the distributor's failure to pay for the merchandise purchased from the supplier, the distributor's own failure to renew and the supplier's withdrawal from the market under certain circumstances. However, identifying in advance what may be considered just cause by a court, jury or arbitrator remains a challenge that will largely depend on the facts of each situation.

In addition, these statutes protect the distributor or sales agent by subjecting the enforcement of typical just cause contractual provisions to a higher standard. For example, under Law 75, the breach of clauses preventing or restricting changes in the capital structure, or in the managerial control of the business, will not automatically constitute just cause justifying termination, unless the supplier shows that such breach may affect, or has truly and effectively affected, the interests of the supplier in the development of the market, distribution of the merchandise or rendering of services in an adverse or substantial manner. Other restrictions exist.

Suppliers should also keep in mind that Law 75 and Law 21 both protect not only against termination without just cause but also against what the laws describe as impairment of the relationship. A classic example of impairment would be sales by a supplier to a distributor, contrary to an agreement of exclusivity with another, who would then argue its rights are being impaired by the sales to the third party.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

Law 75 provides general guidance for the compensation of damages in the event of termination without cause. Law 21 has a similar set of guidelines for compensation of sales representation that is terminated without just cause, but it also has an alternative compensation section that allows, at the request of the sales representative, an alternate compensation calculation: an amount that shall not be greater than 5 per cent of the total sales volume for the years of representation. The court has the discretion of modifying the compensation to ensure it does not constitute an unfair enrichment at the expense of the supplier. In establishing the amount of the alternate compensation, the court shall mainly take into account the compensation received by the sales representative from the supplier and the number of years and sales volume that the sales representative produced during said relationship.

The final determination of damages and entitlement to compensation, however, will ultimately have to be reached by a judge, jury or arbitrator after pondering whether actual damages have been suffered by the distributor or sales representative. The distributor or sales representative will have the burden of proving its damages.

Under Law 75, a court may allow attorneys' fees and a reasonable reimbursement of expert fees to the prevailing party. Law 21, however, has no such provision.

Suppliers should also be aware that, in litigation under both statutes, a distributor or sales representative has a right to request, in addition to damages, a provisional remedy to preserve the status quo of the relationship pending resolution of the litigation. The request is similar to one for injunctive relief and the courts tend to apply similar tests, although the dealer is typically not required to meet the high burden of an ordinary injunction. The court or other decision maker, however, needs to take into consideration the interests of both parties in ruling on the injunction.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

See question 9. The violation or non-performance by a distributor of a provision in a contract preventing or restricting the transfer of the distribution rights, all or part of the ownership of the distributor or agent or the distributor's or agent's business to a third party will not be held valid as just cause for termination of a distribution agreement unless the supplier shows that such non-performance may affect or has truly and effectively affected the interest of the supplier in a substantial manner in the development of the market, distribution of the merchandise or rendering of the service. The supplier bears the burden of proof.

Regulation of the distribution relationship**12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?**

Confidentiality provisions in distribution agreements will be enforced in Puerto Rico under the general contracts law in the Civil Code. They will be considered valid unless they are contrary to law, public order or morals. To date, there is no law that has prohibited or limited these confidentiality clauses in distribution agreements.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

Clauses that restrict the distribution of competing products during the term of the relationship are enforceable in distribution agreements. After the relationship concludes, such competition restrictions will be enforceable if the court determines that they are reasonably necessary to protect the legitimate interests of the supplier. Such determination will be made on a case-by-case basis. Courts have found that a non-competition clause that survived the termination or expiry of a franchise agreement for two years was enforceable (*Franquicias Martín's BBQ, Inc v Luis García de Gracia*, 178 DPR 978 [2010]).

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

Federal antitrust law applies in Puerto Rico. Puerto Rico has its own competition statutes that generally mirror those in the United States both in language and interpretation.

In general terms, and under existing US Supreme Court law, a supplier should be able to impose the vertical restraints of maximum resale price maintenance (RPM) and minimum RPM, although the latter continues to be the subject of diverse positions among state enforcement authorities in the continental United States.

Federal and local enforcement of, or opinion on, the prohibition of either of the forms of RPM is not pervasive in Puerto Rico, unless part of a nationwide US effort that is of high public profile. Therefore, in very general terms, the larger the companies and the more widespread their reach around the world, the higher the possibility that institutional or governmental involvement may occur to scrutinise the pricing structure or mechanisms of the parties.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

See question 14. If a supplier wishes to implement the use of a minimum advertised price policy, it is preferable that the policy be in place beforehand so that if the dealer is not in agreement, the supplier may determine not to deal with the dealer or negotiate the matter. Once the policy is agreed with the dealer, the situation may be more difficult to navigate. Also, it is the view of many that if a minimum RPM is to be established, it should be the supplier doing so as opposed to the distributor.

The use of other mechanisms of vertical restraint that are not so heavily scrutinised may also achieve the intended pro-competitive purposes with lesser legal exposure risk.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

See questions 14 and 15. A distribution contract may specify that the price to a distributor will be equal to those of other distributors, but such a provision should also be included and complied with in contracts with the other distributors, to avoid potential price discrimination exposure.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

See questions 14 to 16. This question seems to contemplate sales at different distribution levels. In general, prices should be the same at the same level, but vertical price restraints are permissible on a case-by-case basis, as much depends on the situation of each circumstance. Volume discounts, for example, are common, but they should be made available to all customers on the same level of distribution, unless other factors justify a difference (eg, additional services rendered by one customer versus the others).

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

See questions 14 to 17. All the vertical restrictions mentioned in the question are generally allowed and ideally should be specified in writing at the time of contracting.

Exclusive territories are permitted but a supplier may just as well restrict the geographic areas or categories to which its distribution partner resells, although in smaller countries or markets enforcement of geographic limits tends to be difficult. The supplier, however, also has the contractual ability to limit the specific market sectors or outlet location areas where the distributor may sell its products. The supplier may also limit within such authorised locations the categories of products to be sold or even the specific products within those categories.

A supplier may reserve certain customers to itself, but it is recommended that the distribution agreement specifically identify such reserved clients and specify the right to modify the list of reserved clients. A supplier may also, in the case of non-exclusive contracts, reserve the right to sell the products in the territory along with the distributor.

Unless specified by contract, we know of no statutory restrictions related to active as opposed to passive sales efforts.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

A supplier may prohibit or restrict e-commerce sales by a distributor either within or outside the assigned territory. The parties may also agree on reporting obligations and the payment of fees or penalties for breach of the restrictions or prohibitions. These restrictions, prohibitions, fees and penalties should be specified in the contract as an essential obligation for a better likelihood of enforcement.

Restrictions on third parties to which the distributor sells are more difficult to enforce, however, usually owing to lack of privity. A supplier may attempt to impose such restrictions by demanding that the distributor include them in its contractual provisions with the third-party intermediaries.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

A supplier can adopt its own sales policy in Puerto Rico and, as such, deal only with the customers it chooses. A supplier may also, as discussed above, contractually restrict to some extent a distributor's right to deal with certain customers. There are of course other laws beyond the scope of this chapter that could prohibit a seller from discriminating against customers for reasons such as age, gender and national origin, for example. Other laws prohibit sales of certain products to sectors of the population (such as minors) owing to the nature of the products.

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

A distribution or agency agreement may be deemed a reportable transaction under merger control rules if its effect is to substantially reduce competition or create a monopoly. The standards used by the Puerto Rican courts to evaluate such a transaction include the following:

- proof that the company (unilaterally or in combination with others) had a specific intent to monopolise the market by controlling prices or lessening competition;
- anticompetitive or predatory conduct was carried out to fulfil such intent; or
- that there exists the probability that such intent be successful.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

Distribution relationships in Puerto Rico are governed by US antitrust laws. Some of these laws have counterpart local statutes, such as the Puerto Rico Antitrust Act 10 PR Laws Ann. sections 257 et seq and the regulations promulgated by DACO that relate to unfair or deceptive practices. The Puerto Rico Department of Justice, through its Office of Monopolistic Affairs, is in charge of enforcing local antitrust policies.

These laws and agencies may affect the distribution relationship depending on the circumstances. Price discrimination issues, for example, would be covered by the Robinson Patman Act.

Private parties may bring actions under the Puerto Rico Antitrust Act. A plaintiff may recover three times the amount of damage in addition to costs and attorneys' fees. Actions must be filed within four years of the occurrence of the cause of action.

An injunction may also be filed to prevent losses or damages to the business or property.

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

Generally, distributors or agents may not be able to detain shipments of diverted 'grey market' products if they are genuine, non-counterfeit goods. A supplier, by itself or with the assistance of the distributor, may be able to keep track of diverted products that are shipped into Puerto Rico and then attempt to stop the product at its source, a task not often easily accomplished.

The supplier and distributor should clarify in their contracts their respective obligations as to both incoming and outgoing diverted products and should request legal advice on how to achieve the best possible result in that endeavour and to define their respective contractual obligations towards each other in case of situations with parallel or diverted products.

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

Advertisement restrictions are imposed by DACO. This agency regulates and inspects periodically on the form of the advertisement and the offer of products to remain vigilant to deceptive and false advertising.

There are no restrictions on a supplier passing on all or part of its cost of advertising on to its distribution partners or sharing its cost of advertising. In fact, a distributor's share in the cost of advertising increases the opportunity that Law 75 will apply to its relationship with the supplier.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

Intellectual property protection in Puerto Rico is similar to that in the United States. Protection exists under both local and federal statutes.

In terms of trademarks and service marks, the basic manner of establishing rights to a mark is the actual use of the mark. Registration of the mark is not required to establish ownership, but it is recommended because it establishes proof of ownership. If the mark will be used in Puerto Rico as well as other places in the United States, registration at the local and federal level is recommended.

In addition to the benefit of protection under US copyright laws, Puerto Rico also has copyright legislation protecting moral rights of the author of a work. The law establishes that registration is not necessary to protect an author's moral rights over its work but, as with trademarks, registration constitutes prima facie evidence of the validity of the moral rights of the author.

Trade secrets are also protected under local law and their owner may seek damages for violation of any dissemination of such secrets. Patents are applied for before the US Patent Office and are protected by US patent laws.

The supplier may file an infringement claim before the courts to enforce its rights to its intellectual property.

Technology-transfer agreements are not as abundant as other types of distribution, assignment or licensing agreements but certainly take place within the Puerto Rican market, with increasing frequency.

26 What consumer protection laws are relevant to a supplier or distributor?

Consumers are protected by regulations promulgated by DACO. The Regulation against Deceptive Practices and Advertisements protects consumers against practices and advertisements that create a false or misleading appearance on goods and services offered to consumers. The regulation also establishes consumer rights in connection with 'rain checks', rebates, warranties and requests for personal information. Suppliers and distributors that wish to conduct sweepstakes or other promotional contests or campaigns as a way of endorsing or supporting the sale of their products will be subject to the Regulation on Sweepstakes, which requires specific information to be disclosed to the consumer and procedures for the execution of the sweepstake.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

There is no specific local legislation for the recall of products but consumer rights will be protected under the general DACO regulations and policies. The distribution agreement may delineate the party responsible for carrying out and absorbing the cost of the recall.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

The extent of the limitation will depend on the nature of the product sold. For example, under the Motor Vehicle Warranty Act, PR Laws Ann. Title 10, sections 2051 to 2065 and DACO's Motor Vehicle Warranty Regulations, every manufacturer must extend the factory warranty to every new motor vehicle registered in Puerto Rico, regardless of where and from whom the consumer acquired it. The warranty to be extended and honoured in Puerto Rico must not be inferior in its terms and conditions to the warranty extended by the maker or manufacturer in benefit of the consumer on the US mainland or in the country in which the motor vehicle was manufactured.

Once a supplier extends a warranty over its product, the distributor must comply with the requirements imposed by the Regulation against Deceptive Practices and Advertisements in connection with the advertisement of such warranties to the consumer.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

The federal rules and regulation that protect consumer privacy and consumer personal information, such as those provided by the Federal Trade Commission, apply in Puerto Rico. See, for example, 16 CFR sections 313.1 to 313.18. In addition, under the Regulation against Deceptive Practices and Advertisements, a distributor cannot obtain personal information of any consumer unless such information is voluntarily provided by the consumer and the consumer is advised as to the use that will be given to such information. The information provided by the consumer on a voluntary basis may not be used to promote offers through telemarketing, unless the consumer has expressly consented in writing to such use. The distributor must take the necessary measures to protect the privacy, confidentiality and integrity of the personal information provided by the consumer. The distributor must also notify the consumer of security breaches of personal information.

Under the EU *Schrems* decision, if suppliers or distributors collect personal identifiable information of an EU person, the supplier or distributor should protect such information in accordance with EU data protection laws. If the supplier is self-certified under the Privacy Shield regime, it must comply with the privacy principles under such regime.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

Suppliers and distributors are generally required to be independent from each other for Law 75 or Law 21 to apply, but a distribution agreement may require a distributor to maintain a certain type of management structure, ownership or standards of quality. However, under Law 75, a supplier will not have just cause to terminate the distribution relationship owing to a change in the distributor's management unless the distribution agreement provided specifically for that possibility and the supplier can show that the breach will substantially and adversely affect (or has affected) the distributor's interests in the development of the market, the distribution of the merchandise or rendering of the services in question. The supplier will bear the burden of proof to show such injury. The supplier's vetting, approval or disapproval of employees of the distributor, or of their actions, could potentially subject the supplier to employer liability alongside the distributor.

Update and trends

Act 257, enacted 10 December 2018, reduces the corporate income tax for taxable years commencing after 31 December 2018 to rates that would range between 18.5 and 37.5 per cent. Capital losses incurred after taxable year ending 31 December 2018 are allowed up to 90 per cent of the net capital gain generated in the taxable year and can be carried forward until exhausted subject to the 90 per cent limitation.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

The interaction between the supplier, the distributor and the distributor's employees, as a whole, will be analysed to determine whether an employment relationship exists. Various factors will be taken into consideration to determine the existence of an employment relationship.

The determining factor is that of control retention. An employment relationship exists where the principal or supplier has the right to control the contractor's, the distributor's or the distributor's employees' work not only as to the end result, but also as to the manner and means by which the result is accomplished. Examples of control include, but are not limited to, the ability to approve or deny overtime, payment of bonuses and designation of employees to work in specific capacities.

The risk of having a distributor as an employee of the supplier is that the supplier will be exposed to Puerto Rican and US labour and employment legislation.

A supplier can take various measures to avoid creating employee relationships with its distributors, among which are the following:

- the distributor should be free to engage in other enterprises or economic activities;
- the distributor should have an employer social security identification number;
- the distributor should obtain its own workmen's compensation insurance policies;
- the distributor should determine his or her own schedule of work and that of its employees; the supplier should not require specific days or hours of service;
- the supplier should not supervise the manner in which the distributor renders its services; and
- the supplier may only pass judgement on end results to determine whether the service relationship is beneficial to the supplier.

32 Is the payment of commission to a commercial agent regulated?

No, but general tax withholding obligations will apply to such payments.

33 What good faith and fair dealing requirements apply to distribution relationships?

Good faith and fair dealing requirements apply to all contractual relations, including the negotiation, performance and termination of distribution relationships.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

No.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

Anti-bribery or anti-corruption laws apply to relationships between suppliers and their distribution partners in the event that they involve making payments or providing anything of value to government officials to assist in obtaining or retaining business.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

In addition to the restrictions set forth under Law 75 already discussed, Law 75 provides that the rights granted under that statute cannot be waived. See restrictions on choice of law and forum selection clauses in questions 37, 38 and 40.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

Distribution and sales representation contracts must be interpreted pursuant to and governed by the laws of Puerto Rico, and any other stipulation to the contrary will be void. The use of arbitration agreements to settle disputes may affect this provision, particularly when the arbitrator is given broad powers and depending on how the arbitration clause is negotiated and drafted.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

Although Law 75 originally prohibited arbitration outside Puerto Rico, that prohibition is no longer valid. Forum selection clauses, on the other hand, requiring the parties to litigate in Puerto Rican courts, have been enforced on some occasions but not on others. The issue remains an open question to be decided on a case-by-case basis where Law 75 is concerned.

Under Law 21, however, the courts are more likely to uphold forum selection clauses and arbitration outside Puerto Rico is similarly not prohibited.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

Puerto Rico has its own judicial system consisting of a Court of First Instance, appellate courts and the Supreme Court of Puerto Rico. Parties may also have access to the US District Court for the District of Puerto Rico, a federal court sitting in Puerto Rico with the same powers and jurisdiction as similar courts in the United States.

Both suppliers and distributors have equal access to either of these courts, with the main restriction being the existence of federal jurisdiction for litigation in federal court. This requisite will generally be met

in the case of foreign suppliers. Foreign suppliers will also need to post a non-resident bond in local Puerto Rican courts to secure payment of costs or attorneys' fees. Such bond is not required by rule in federal courts. Either court must, of course, also have personal jurisdiction over the parties in the litigation.

Both court systems may provide relief in law and equity, such as the provisional remedy discussed in question 10.

Foreign suppliers can expect fair treatment in either court system. Under both systems, litigants may require disclosure of documents or testimony before trial. An important difference between the two systems is that a jury is not available in civil or commercial disputes brought in local Puerto Rican courts whereas jury trial is available for those types of disputes in federal court.

There are no particular advantages or disadvantages to a foreign business resolving disputes in Puerto Rican courts, except for those that any party would encounter or perceive when litigating in a foreign country, such as the costs and burden of attending proceedings away from home and under perhaps quite different procedural rules, hiring and working with local counsel and dealing with the generally perceived notion that a local court might favour the local party owing to some type of national or territorial prejudice or protectionism. Both of the systems in Puerto Rico, however, are predicated on tenets of due process of law, like those underlying dispensation of justice in the United States and other countries.

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

An agreement to arbitrate disputes will likely be enforced in Puerto Rico. If the dispute is brought under Law 75, however, before the dispute is submitted to arbitration any of the parties must request that a court with jurisdiction in Puerto Rico determine that said clause or arbitration agreement was subscribed freely and voluntarily. Law 75 also creates a rebuttable presumption that any arbitration agreement or clause in a distribution agreement was included or subscribed at the request of the supplier and is an adhesion contract.

There are no limitations (such as on the arbitration tribunal, the location of the arbitration or the language of the arbitration) on the terms of an agreement to arbitrate.

The main advantage of arbitration for a foreign entity is the opportunity to reach an agreement with the local distributor or representative to resolve a dispute outside Puerto Rico and under a law other than Puerto Rican. It is always possible, however, that a court or arbitrator may end up deciding to apply Puerto Rican law regardless of the agreement of the parties. The choice of forum for the arbitration, however, is most likely to be enforced either by courts or arbitration tribunal.

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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

Yes, a foreign supplier may establish its own entity with no greater restriction than a Turkish national in accordance with article 3 of Foreign Direct Investment Law No. 4875, and will be subject to Turkish Commercial Code (TCC) No. 6102, as are Turkish nationals.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Yes, there is no specific restriction with regard to foreign suppliers in this respect.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

In practice, the best suited type of business entities for foreign suppliers would be in the form of a joint stock company or a limited liability company. These companies are preferable, as the liability of the shareholders of these companies is limited to the capital that is committed to the company.

A joint stock company and a limited liability company can be established by at least one or more shareholders who can be real persons or legal persons. These two types of companies are different with regard to the minimum required amount of capital. The capital of joint stock companies shall not be less than 50,000 Turkish liras. For limited liability companies, the capital of the company shall not be less than 10,000 Turkish liras.

To establish a joint stock company or a limited liability company, articles of association shall be filed with the Central Registry Record System (MERSIS) and be signed by the founders, or via power of attorney, with the Trade Registry Office's authorised personnel. In addition to the articles of association, other company documents that are required for the establishment shall be submitted to the relevant Trade Registry Office. The capital shall be paid in accordance with the provisions of the TCC. For the joint stock companies, one-quarter of the subscribed share capital must be paid in cash prior to the registration of the company and the remaining part must be paid within 24 months following the registration of the company. Alternatively, the capital may be fully paid prior to the registration. However, the requirement to pay one-quarter of the capital before the registration of the company is not applicable to limited liability companies. Thus, subscribed capital for limited liability companies must be paid within 24 months following the registration of the company. When all of the required documents are duly submitted, the establishment of the company shall be registered with the relevant Trade Registry and, finally, the establishment shall be announced in the Trade Registry Gazette. Additionally, pursuant to article 64 of the TCC, during the registration of the joint stock companies and limited liability companies, opening approval of the company books shall be processed through the directorates of the Trade Registry.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

Unless otherwise stated in international agreements or special laws, foreign investors are free to invest in Turkey and be subject to the national treatment principle. In other words, they have equal rights and obligations as have national investors. Law No. 4875 does not stipulate any restriction with regard to the branches of industry in which foreign businesses may operate.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

Yes, as explained in question 4, foreign suppliers have equal rights and obligations with regard to national suppliers, according to Law No. 4875.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

The Turkish direct taxation system is comprised of two main taxes, those being personal income tax and corporate income tax. An individual is subject to personal income tax on his or her income and earnings in line with the provisions of Income Tax Code No. 193 (ITC). Corporations are subject to corporate income tax as per provisions of Corporate Tax Code No. 5520 (CTC).

Taxation of corporations: Resident companies with unlimited tax liability would be taxed on their worldwide income in Turkey. Non-resident companies with limited tax liability are subject to tax only on Turkish-sourced income. The former standard corporate tax rate of 20 per cent is increased to 22 per cent for the fiscal periods of 2018, 2019 and 2020. Additionally, withholding tax is applied on dividends, interests, royalties and technical services fees. The withholding tax rate varies depending on the type of the payment and the provisions of the relevant double tax treaty.

Taxation of individuals: Resident individuals are taxed on worldwide income; non-residents are taxed only on Turkish-source income. Taxable income is comprised of employment income, business income, income from agricultural activities, professional income, income derived from shares, income from immovable property and other income (capital gains and non-recurring income). Individual income tax rates apply on a progressive basis, ranging from 15 per cent to 35 per cent.

Stamp tax is also another tax burden in Turkey. In accordance with the Stamp Tax Code No.488 (STC), any legal documents (papers) signed in Turkey, or signed abroad where the beneficial interest of the parties lies in Turkey, will be subject to stamp duty, unless there is an applicable exemption. In principle, stamp tax is levied as a percentage of the value stated on the agreements at rates varying between 0.189 and 0.948 per cent (unless a specific rate is determined, the general rate for commercial agreements is 0.948 per cent). The STC also provides for a cap on the amount of stamp duty payable, which is adjusted on a yearly basis. For Fiscal Year 2018, the stamp duty cap is 2.135.949,30 lira.

Apart from the above-mentioned tax liabilities, the Turkish taxation system comprises several indirect taxes, but the most important ones are the value added tax (VAT) and special consumption tax (SCT). Liability for VAT arises; (i) when a person or entity performs commercial, industrial, agricultural or independent professional activities within Turkey, (ii) when goods or services are imported to Turkey. VAT is levied at each stage of the production and the distribution processes. However, the real VAT burden is on the final consumer. In principle, the following persons or entities are liable for VAT: those supplying goods and services; and those importing goods or services. In the event that the taxpayer is not resident, or does not have a place of business, a legal head office or place of management in Turkey, or in other cases as deemed necessary, the Ministry of Finance is authorised to hold any person who is involved in a taxable transaction responsible for the payment of tax. VAT rates vary from 1 to 18 per cent, depending on the type of the goods and services subject to delivery.

SCT is levied only once at one stage of the consumption process of the goods within the scope of four lists annexed to SCT Law No. 4760. The goods subject to taxation are indicated through tariff codes generated from the Turkish Customs Tariff Nomenclature (TCTN). The TCTN is in compliance with the Combined Nomenclature, which is the international classification system for goods.

Additionally, it should be noted that double tax treaty provisions should also be taken into consideration when making a final conclusion in terms of taxation principles.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

There are several distribution structures available to a supplier. The most common ones are those described below.

Distributors buy goods from their principal and sell them directly to their own customers on their own behalf, and at their own risk, and are remunerated through a margin. There is no specific legislation regarding distribution agreements. If there are disputes between the parties as to a distribution agreement, then the provisions of the sales agreement, the agency agreement, proxy or service agreement shall apply by way of analogy, depending on the legal matter that is to be decided.

Agents are intermediaries who promote the conclusion of agreements, negotiate agreements between the principal and the customer, at no risk to themselves, and are entitled to a commission. Commercial agency agreements are regulated under articles 102 to 123 of the TCC.

Sales representatives undertake the obligation to mediate in the process of transactions, or conclude agreements or make transactions set forth in the agreement, concluded between the merchant and themselves, in the name and on behalf of the merchant, consistently and outside the business, in return for payment. By concluding a sales representation agreement, a relationship of dependent merchant assistance shall be established between the parties.

Joint venture agreements, which qualify as ordinary partnership agreements, are subject to the provisions of Turkish Code of Obligations (TCO) No. 6098. As joint venture agreements are not exclusively regulated under Turkish law, they are not subject to any formal requirement.

Although there is no specific legislation, or any regulation governing franchise agreements under Turkish Law, a franchising contract can also be concluded, and it is commonly used in Turkish commercial practice.

Moreover, licence agreements can be concluded in accordance with Industrial Property Law No. 6769. Accordingly, industrial property rights, except geographical indications and traditional speciality guarantees, may be subject to licensing.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

Agency agreements are regulated by the TCC in articles 102 to 123, sales representation agreements are defined and regulated under the TCO, trademark licensing agreements are regulated under Law No. 6769, and joint venture agreements, which qualify as ordinary partnership agreements, are subject to the provisions of the TCO. Although franchise agreements are not explicitly defined under Turkish legislation,

they can be concluded as sui generis agreements, and provisions of the TCO and TCC regarding sales, agency, service and proxy agreements apply to franchise contracts by way of comparison. There is no specific legislation regarding distribution contracts. The TCO does not regulate exclusive distribution agreements or distribution agreements. If there are disputes between the parties to a distribution agreement, then the provisions of agency agreements, sales agreements, and proxy or service agreements shall apply by way of analogy depending on the legal matter that is to be decided. Also, the general provisions of the TCO, as the case may be, as they relate to agreements, may apply when appropriate, especially in the event of any breach of contractual obligations and default.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

As per the TCC, either party to an agency agreement may declare the termination of an indefinite-term agency contract by giving three months' prior notice to the other party. In accordance with Turkish legal practice, this three-month notice period also applies to distribution contracts. Additionally, it is possible for a party to claim compensation for damages arising out of the unjust termination of a contract or without having received three months' prior notice.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

Article 122 of the TCC stipulates the goodwill indemnity, also known as goodwill compensation, in terms of commercial agency agreements. Pursuant to the fifth paragraph of this article, this provision shall also be applied in exclusive distribution agreements, as well as in other continuous contractual relationships that grant similar exclusive rights. In this respect, after the termination of the contractual relationship, the agency may claim reasonable compensation from the principal (i) if the principal, after termination of contractual relationship, continues to derive substantial benefits from the new customers that the agent has brought to the principal; (ii) as a result of the termination of the agency agreement, if the agent loses its right to demand commission that would have been obtained from the agreements entered into or to be entered into within a short period of time with the new customers, if the contractual relationship has not been terminated; and (iii) if payment of the compensation is equitable by taking into consideration all circumstances in question.

The goodwill compensation may not exceed a figure equivalent to the average of the annual commissions or other payments made to the agent as a result of its activities in the last five years. If the agency agreement continued for less than five years, then compensation shall be calculated on the average for the period in question. However, the agency shall not be entitled to claim compensation if the agent terminates the agency agreement, unless the termination is justified by circumstances attributable to the principal, or if the principal due to a default attributable to the agent terminates the agency agreement. Additionally, pursuant to article 122(4) of the TCC, the parties may not derogate from the goodwill indemnity prior to the expiry of the agency agreement.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

The parties may stipulate in their agreement that the supplier may transfer the products to the distributor, without transferring the right of ownership of the products. This is referred to as the 'sale with retention of title' clause under Turkish law. The retention of title clause is regulated under article 764 of Turkish Civil Code (CC) No. 4721. Accordingly, ownership of a good that has been transferred to a distributor may be retained if a notary in the transferee's place of residence registers the transfer agreement that is subject to official form with the special registry.

Transfer of the commercial business is regulated both under the TCO (articles 202 and 203) and the TCC (article 11(3)). The said

provisions do not stipulate any requirement of approval to be given by the supplier in order to be able to transfer the business to a third party. Nevertheless, the parties may stipulate such restrictions within the framework of the contractual freedom. Likewise, the parties may also stipulate the scope and results of change of control in their agreement, and such clauses will be enforced under Turkish law.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

Under the distributor's loyalty obligation to the supplier, the distributor has a confidentiality obligation regarding trade secrets and confidential information regarding works and workshops. Thus, the Turkish courts shall enforce confidentiality provisions so long as the scope of these provisions comprise the protection of trade secrets of the business of the supplier.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

Restrictions on the distribution of competing products in distribution agreements may be enforceable provided they are in compliance with Turkish competition law.

Pursuant to Block Exemption Communiqué on Vertical Agreements No. 2002/2 (Communiqué No. 2002/2), agreements concluded between two or more undertakings that operate at different levels of the production or distribution chains, with the aim of purchasing, selling or reselling particular goods or services that are referred to as vertical agreements, as well as including the distribution agreements, are exempted in block from the prohibition in article 4 of the Law on the Protection of Competition No. 4054. The exemption granted shall apply in the event that the market share of the provider in the relevant market in which it provides the goods or services that are the subject of the vertical agreement does not exceed 40 per cent.

The exemption granted by Communiqué No. 2002/2 shall not be applicable if non-competition obligations imposed on the purchaser are for an indefinite period, or whose duration exceeds five years. Thus, distribution agreements with non-competition obligations for an indefinite period, or those that exceed five years, are deemed to restrict competition and are considered to be unlawful.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

As per Turkish competition law, the supplier's setting of fixed or minimum sales prices for the buyer is strictly prohibited. However, the supplier may set maximum sales prices for the buyer, or offer recommended sales prices to the buyer, provided these do not transform into fixed or minimum sales prices. Where the supplier's market share does not exceed 40 per cent, recommended price and maximum price practices are evaluated within the scope of block exemptions. In order to ensure that maximum or recommended sales prices as notified to the buyer do not become minimum or fixed prices, price lists or packaging of the product must clearly state that the prices concerned are the maximum or recommended prices.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

Besides directly maintaining resale prices through the inclusion of explicit provisions in signed vertical agreements, suppliers may also commit the same violation, indirectly, through various practices, such as: (i) setting the profit margin of the buyer; (ii) setting the maximum rate of discount that may be implemented by the buyer over a recommended price level; (iii) providing discounts to the buyer to the extent that the buyer complies with recommended prices; (iv) threatening the buyer with delaying and suspending deliveries; (v) terminating the agreement if the buyer does not comply with those recommended prices; or (vi) the actual implementation of such penalties.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

Most-favoured-nation (MFN) clauses are commonly found in a wide range of commercial agreements from long-term industrial supply to distribution arrangements, and are allowed under Turkish competition law, provided that they do not hinder competition in the relevant market. Although there were no specific provisions regulating MFN clauses under Turkish competition law prior to 2018, as a result of a recent amendment to the Guideline on Vertical Agreements in 2018, MFN clauses are now formally recognised and regulated. In this regard, such clauses benefit from block exemptions under Communiqué No. 2002/2 if the beneficiary has a market share less than 40 per cent. It is emphasised in the Guideline on Vertical Agreements that in competition law assessments involving MFN clauses, the market positions of the party benefiting from the clause, as well as its competitors, the purpose of including the clause in the agreement, and the characteristics of the market and the clause, must all be examined in detail. Furthermore, the Turkish Competition Board has particularly been interested in MFN clauses in online platform agreements and has recently rendered two decisions with respect to MFN clauses, concluding that broad-MFN clauses violate competition and would not benefit from individual exemption; whereas, narrow MFN clauses may be justifiable in certain cases.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

Vertical agreements that involve limitations, such as introducing restrictions in relation to regions or customers where, or to whom, the goods or services that are the subject of the agreement shall be sold by the purchaser, and whose goal is to hinder competition, directly or indirectly, may not benefit from the exemption granted by Communiqué No. 2002/2. In this respect, excluding the following four exceptions, region or customer restrictions may not be imposed upon purchasers:

- provided that it does not cover sales to be made by customers of the purchaser, restrictions imposed by the provider of active sales to an exclusive region, or exclusive group of customers assigned to it or to a purchaser;
- restriction of sales of the purchaser operating at the wholesale level in relation to end users;
- restriction of the performance of sales by the members of a selective distribution system to unauthorised distributors; and
- if parts are supplied with a view to combining them, restriction of the purchaser's selling them to competitors of the provider who is the producer.

To be in compliance with competition law, the seller may charge different prices to different customers by way of introducing restrictions in relation to regions or customers.

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

Please see question 17.

The protection provided to undertakings via granting an exclusive region or customer group is not absolute. When selling to the region or customer group assigned to them, buyers can only be protected from active competition by the other buyers within the system. In other words, the supplier may restrict active sales to exclusive regions or customer groups assigned to it or to a buyer. However, restriction of passive sales to that region or customer group shall be considered an infringement that excludes the agreement from the block exemption.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

Pursuant to the recent amendments to the Guideline on Vertical Agreements in 2018, the Turkish Competition Authority has

implemented a broad regulation based on the European Commission's Guidelines on prohibitions on online sales. As per the Guideline on Vertical Agreements, limitations imposed on online sales will exclude vertical agreements in question from the scope of block exemptions. These limitations, in particular, are: restrictions imposed on buyers with regard to territory and customers to which the contractual goods and services will be sold; restrictions on the proportion of sales made via the internet; and limitations of determining higher prices to be paid by the buyer for products to be sold on the internet other than the products to be offered at the physical point of sale.

Furthermore, the Guideline on Vertical Agreements regulates that the provider may set forth certain conditions with respect to the use of the internet as a sales channel. These conditions are exemplified as follows: the quality conditions for the website in which the products are offered for sale; the requirement of providing certain services to online consumers; and the obligation to maintain a physical point of sale. Also, in accordance with the Guideline on Vertical Agreements, provided that the online sales are not prevented, directly or indirectly, the provider may request that the buyer sell through the 'sales platforms' that meet certain standards and conditions.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

Under Turkish competition law, undertakings, whether in a dominant position or not, are in principle not obliged to conclude contracts with other undertakings, in line with the principle of freedom of contract. In other words, any undertaking, whether or not dominant, should have the right to choose its trading partners and to dispose freely of its property. However, in some cases, undertakings in a dominant position are under the obligation to conclude contracts in opposition to the principle of freedom of contract. This obligation is referred to as the essential facilities doctrine. Based on this obligation, the owners of an essential facility must enable their competitors or customers to access that facility.

Refusal to supply may be related to competitors or non-competitive clients in a downstream market. A supplier may restrict its distributor's ability to deal with particular customers on the condition that an exemption is granted under competition law (see question 18).

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

The Turkish Competition Authority is entitled to control significant concentrations. Pursuant to article 5 of the Communiqué on Mergers and Acquisitions Subject to Approval of the Competition Board, (i) the merger of two or more undertakings, or (ii) the acquisition of direct or indirect control over the whole or a part of one or more undertakings, by one or more undertakings, or one or more persons who currently control at least one undertaking, by way of purchasing shares or assets, through a contract or through any other means shall be considered a merger or acquisition transaction, provided there is a permanent change in control.

Pursuant to article 7 of the Communiqué, approval of the Competition Board is required in order to gain legal validity, where: (i) the total turnovers of the transaction parties in Turkey exceed 100 million Turkish liras, and turnovers of at least two of the transaction parties in Turkey each exceed 30 million Turkish liras; or (ii) the asset or activity subject to acquisition, and at least one of the parties in merger transactions have turnover in Turkey that exceeds 30 million Turkish liras, and the other party of the transactions has a global turnover that exceeds 500 million Turkish liras.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

In general, antitrust law prohibits any agreements that intend to, or result in, restraint of competition. In the selective distribution system,

the following restriction limitations, the goal of which is to hinder competition, directly or indirectly, may not benefit from the exemption granted by Communiqué No. 2002/2: (i) restriction of active or passive sales to end users, to be performed by system members operating at the retail level, provided that the right is reserved as to the prohibition for a system member against operating in a place where he or she is not authorised; and (ii) prevention of purchase and sale between system members themselves.

Competition law is mainly enforced by the Turkish Competition Authority, especially through fines. Private competition law enforcement in Turkey is regulated under articles 57 et seq of Law No. 4054. In accordance with article 57, anyone who prevents, distorts or restricts competition via practices, decisions, contracts or agreements that are contrary to Law No. 4054, or abuses their dominant position in a particular market for goods or services, is required to provide compensation for any damages suffered.

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

The supplier cannot prevent parallel or grey market imports after the products have been supplied to the market. Article 152(1) of Law No. 6769 stipulates that acts related to the products that are subject to protection of industrial property rights shall fall outside the scope of the rights, where such acts occurred after those products have been supplied to the market by the right owner or third parties who are authorised by it.

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

Advertisements that are in violation of the principle of good faith are restricted under TCC article 55/1(a). Accordingly, advertisements that slander competitors by making incorrect, misleading or unnecessarily harmful statements about their products, prices, commercial operations and so forth are prohibited. Moreover, providing incorrect or misleading information about oneself, or one's products and services, is considered to be unfair and illegal.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

Law No. 6769 regulates industrial property rights that are trademarks, geographical indications and traditional product names, designs, patents and utility models. In order to safeguard its intellectual property from infringement by its distributor partners and by third parties, a supplier should register its intellectual property with the Turkish Patent and Trademark Office. Registered intellectual property rights are protected by *lex specialis*, Law No. 6769. The supplier may exercise the relevant rights in the event of infringement, such as requesting indemnification of pecuniary and non-pecuniary damages, claiming for damages suffered, including actual loss and loss of profit. Nonetheless, the general provisions under the TCC's unfair competition rules protect unregistered intellectual property rights.

Technology-transfer agreements are also commonly used in Turkey, whereby the intellectual property rights that are licensed are basically regulated within the framework of the legislation relating to those rights. The said legislation allows for provisions, such as the granting of exclusive licences, which may be restrictive towards competition under certain circumstances, to be included in technology-transfer agreements. In this context, the Block Exemption Communiqué Relating to Technology Transfer Agreements exists, which provides for the conditions whereby the provisions, contained in technology-transfer agreements, and which are restrictive of competition under article 4 of Law No. 4054, are granted an exemption, when they are accepted to satisfy the requirements under article 5 of Law No. 4054.

26 What consumer protection laws are relevant to a supplier or distributor?

The Law on Protection of the Consumer No. 6502 defines the provider as a real or legal person that provides services to the consumer

with commercial or professional purposes, or acts in the name of, or on behalf of, the service provider, and regulates the obligations of the service supplier with regard to providing defective products to the consumers. Law No. 6502 applies when the other party to the contract is a consumer. Thus, whenever the end customer of a service provider is a consumer, the service provider may be held liable.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

The Law on Preparation and Implementation of Technical Legislation regarding Products No. 4703 constitute the legal basis for market surveillance activities by regulating the supply of products to the market, obligations of producers and distributors, as well as prohibition of the supply of products to the market, and the recall of products. As per Law No. 4703, the producer is obliged to supply safe products to the market and provide necessary information about its content, packaging and possible risks of hazard. Suppliers may only be released from liability if they prove that the product has not been supplied to the market by them, or that the hazard deviated from conformity with technical regulations. The producer shall provide the consumers with the necessary information about the risks of the products, and when necessary, take samples from the products supplied to the market, investigate complaints, inform the distributors of the results of the inspections made, and take the necessary precautions, including the prevention of risks, and the recall and disposal of products. Additionally, the distributors shall not supply unsafe products to the market and they shall fulfil the obligations imposed on them by technical regulations.

However, Law No. 4703 should be revised taking into consideration the updates of the EU acquis. In this respect, to revise Law No. 4703, the Draft Law on Product Safety and Technical Regulations has been prepared and submitted to Grand National Assembly of Turkey on 29 March 2018, but has not yet been enacted as at the time of writing.

Responsibility for carrying out and absorbing the costs of a recall may be delineated by the distribution agreement.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

The parties may limit their liability in their agreements and these types of clauses are enforceable under Turkish law. As the clauses that exclude or limit liability are vital with regard to the parties' relationships, it is recommended that they be written in explicit and clear language. The validity of the clauses that limit liability shall be subject to the general provisions of freedom to contract and nullity of the contract, as regulated under the TCO. In this respect, clauses that limit or exclude liability shall be rendered invalid if they are in contradiction with the principles of good faith.

Moreover, pursuant to the TCO, agreements on exclusion of liability for gross negligence, in advance, are deemed null and void.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

In compliance with the Law on the Protection of Personal Data No. 6698, any operation performed upon personal data (all the information relating to an identified or identifiable natural person) of customers and end users including, but not limited to, collection, recording, storage, retention, alteration, reorganisation, disclosure, transferring, taking over, and so on are only allowed if permitted by law, or by the explicit consent of the data subject (customers and end users). Personal data shall not be transferred without obtaining the explicit consent of the consumers and end users. Nonetheless, pursuant to article 8 of Law No. 6698, personal data may be transferred without seeking the explicit consent of the individual, subject to the existence of one of the conditions in the second paragraph of article 5 (Conditions for processing of personal data) and the third paragraph of article 6 (Conditions for processing of personal data of special nature), provided that sufficient measures are taken. That being said, for the transfer of personal data abroad (ie, outside of Turkey), explicit consent of the data subject is

required. Exceptionally, personal data may be transferred abroad without obtaining the explicit consent of the data subject if certain conditions set forth under Law No. 6698 exist, and if the foreign country to which personal data will be transferred has an adequate level of protection. If there is no sufficient protection in the destination country for realisation of the data transfer, the data controllers in Turkey and in the foreign country must provide a written commitment, stating that sufficient data protection will be provided, and such transfer must be authorised by the Personal Data Protection Board (Board). Countries providing sufficient protection will be determined by the Board; however, by the end of 2018, no such determination has been made.

In general, being independent from the supplier, each distributor owns the data they have gathered concerning the customers and end-users to whom products were resold. Based on the above, regardless of the exceptions provided under article 8 of Law No. 6698, distributors may not transfer any information related to customers and end users without obtaining their explicit consent.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

Provided that the parties explicitly stipulate such approval or rejection right, a supplier may approve or reject those individuals who manage the distribution partner's business. As mentioned earlier, there is no specific regulation regarding distribution agreements under Turkish law. Therefore, in such cases, the relevant proxy provisions may find application, and the supplier may have a right to approve or reject the service in question if it must be rendered by the distributor in person.

Dissatisfaction with management must constitute a justifying and 'important' reason to terminate the distribution relationship. A reason is considered to be important in the event that the continuation of the distribution agreement becomes unreasonable for the party who seeks to terminate the agreement. As it is also accepted in the doctrine, it is impossible to determine all of the reasons that constitute an important reason; therefore, in such cases, the judge shall consider the circumstances of each case. What is decisive in this respect shall be the continuation of mutual confidence.

Another option for the supplier is to terminate the relationship with notice. There are no periods of notice stipulated, especially for distribution contracts. There are those who argue that a three-month period stipulated for agency agreements should be applicable for distribution agreements, as well. However, there is no consensus on this issue. This termination right should be used in accordance with the trust that is created with the distributor.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

As distributors and agents act independently, in principle, they are not treated as an employee of the supplier. Pursuant to article 102(1) of the TCC, commercial agents should not be strictly dependent upon the principal as are its employees. Therefore, under Turkish law, it is explicitly regulated that commercial agents cannot be considered as employees. The relationship between an agent and a principal is deemed as a form of special representation. An agent is legally required to conduct the agency activities in compliance with the principal's instructions, to the extent that such instructions do not infringe upon the independence of the agent.

To distinguish the self-employed agent from the employee, one should examine the order of the activities of the agent and his or her working hours. If the principal gives strict instructions on these topics, then the counter-party is deemed to be an agent, but not an employee. An agent must freely coordinate his or her own business activities.

Although a person concludes a contract under the title of 'agency contract', if he or she has obligations, such as to remain at the workplace for a certain number of hours, to submit reports regularly within short periods, or he or she does not have a separate office, among others, which indicates subordination to the principal, he or she would be considered to be an employee.

Thus, he or she would not be subject to the TCC, but to labour law. Pursuant to Turkish Labour Law No. 4857, an employment agreement

is an agreement whereby the employee independently undertakes to perform work for the employer who undertakes to pay him or her remuneration. In this respect, the dependency element is an important factor in order to determine the employment relationship. It is not always easy to distinguish an agent from an employee where the agent works closely with the principal. In such cases, the distinction should be made by taking into consideration the facts of the case.

In a general sense, a supplier does not need to protect against responsibility for potential violations of labour and employment laws by its distribution partners; however, when distribution partners are dependent upon the supplier, thus, if an employment relationship is established, then the supplier may be held liable in accordance with Law No. 4857.

32 Is the payment of commission to a commercial agent regulated?

Under Turkish Law, in accordance with article 113 of the TCC, the agent may claim commission:

- if the transaction has been intermediated or concluded by the agent personally, and on behalf of the principal; or
- if the transaction has been concluded directly between the principal and a third party within the territory assigned to the agent, and within its exclusive field of activity.

To protect the agent, it is stipulated that the principal is obliged to inform the agent immediately concerning any transaction it has concluded, directly. Pursuant to the TCC, should the above circumstances exist, the agent may even request a commission regarding the agreements concluded after the termination of agency relations, and this can be referred to as a post-termination commission.

There are no provisions in the TCC concerning an agent's right of commission on successive business that is concluded directly by the principal with a third party who was previously acquired as a customer by the agent. A clause stipulating such a right to the agent may be inserted in the agency contract.

The parties are free to agree on the amount of commission. If there are no provisions in the contract, the amount of the commission will be determined according to the trade customs and practices within the territory of the agent, and if such trade customs and practices do not exist, then it will be determined according to other considerations by the court. Additionally, the collection of the commission by the supplier shall not be expected necessarily for payment of the commission, unless otherwise specified in the agreement.

Pursuant to the TCC, the agent has the right to commission the time, and to the extent, that the business is concluded. The parties may agree to different terms in the agency agreement; however, when the principal concludes the business, the agent has the right to a reasonable commission that may be requested on the last day of the subsequent month. In any event, the agent has the right to commission the time, and to the extent, that the third party concludes the business.

33 What good faith and fair dealing requirements apply to distribution relationships?

Pursuant to article 2 of the CC, every person must act in good faith in the exercise of its rights and in the performance of its obligations. According to this provision, the abuse of rights is not protected by the rule of law. This principle shall also apply to distribution relationships. Within this legal framework, specific provisions that are based on good faith may also apply to this relationship. For instance, as there is no specific legislation regarding distribution agreements under Turkish law, and agency provisions may apply to these relationships, the provisions regarding goodwill compensation under the TCC may apply to distribution agreements.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

Pursuant to Law No. 6769, industrial property rights, except for geographical indications and traditional speciality guarantees, may be assigned, be subjected to pledges, and be subject to licensing, and these legal transactions may be registered with the Turkish Patent and Trademark Office. Such legal transactions may be registered at one of the parties' request, and if payment of the fee and other conditions

specified by the regulation are fulfilled. Legal transactions that are not registered with the registry cannot be alleged against bona fide third parties. On the other hand, registration does not have constitutive effect, and is explanatory. In other words, although registration does not have to be affected for the validity of the agreement, it cannot be alleged against third parties unless it is registered.

In terms of distribution agreements, in principle, they do not have to be registered or approved by any government agency.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

Pursuant to Turkish Penal Code No. 5237, penal sanctions cannot be applied to legal persons. However, sanctions that are qualified as precautions, and which are stipulated by law, may be imposed upon legal persons. The main offences regarding corruption and bribery stipulated under the Penal Code are bribery, fraud, embezzlement, laundering of criminal proceeds and bid-rigging. In this respect, pursuant to the Penal Code, security precautions that are specific to legal entities are applicable for those who secure unjust benefit by committing the offence of bribery. As per the Penal Code, in such cases, the licence granted to the company may be cancelled, and the provisions regarding confiscation shall be applied to the legal entities involved in the commission of the offence. Moreover, pursuant to Misdemeanours Law No. 5326, in the event that a body or a representative of a legal person, or a person who undertakes a duty within the framework of the operational field of the legal person, commits this offence an administrative fine of 10,000 to 2 million Turkish liras shall be applied.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

The TCC regulates the contractual non-compete obligation for the period that is subsequent to termination of the agency agreement. Non-competition agreements should be concluded for a maximum of two years. The principal shall compensate the agent for valid non-competition agreements. As provisions of the law regarding agency contracts apply to distribution contracts by comparison, this provision shall also apply to distribution contracts. Statutory law (see question 8) will apply, even if the related provisions are absent from the contract.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

No. The parties may choose any country's law to govern a distribution contract.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

Pursuant to the Turkish Code of Civil Procedure (TCCP) No. 6100, the competent court with regard to place of jurisdiction is the court located at the domicile of the defendant on the date of filing the lawsuit. This is also binding upon the parties of the distribution agreement. Moreover, the courts located at the place wherein the contract is performed, are also accepted as competent under article 10 of the TCCP. On the other hand, if both parties are either merchants or public legal persons, then they can agree upon the competent court with regard to place of jurisdiction under the TCCP; however, real persons, who are not merchants, may not agree upon the competent courts. As mentioned above, there is no explicit reference to distribution contracts in the TCC. However, article 4(1) of the TCC stipulates that disputes arising out of the matters related to the commercial enterprises of each party shall be deemed 'commercial disputes', regardless of whether or not they are merchants. Considering the fact that the distribution agreements are related to the commercial enterprises of the parties, such disputes shall be submitted to the commercial courts pursuant to the said article. Distribution contracts are arbitrable under Turkish law. Therefore, the parties may freely refer their disputes to arbitration.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

Commercial courts are the competent courts with regard to disputes related to distribution contracts (see question 38). Appealing the decisions of commercial courts by referring the case to the Court of Appeals and to the Court of Cassation is possible.

Foreign businesses may refer to the Turkish courts when the rules of Turkish International Private Law and Procedural Law No. 5718 stipulate that the case shall be heard before Turkish courts.

A litigant may require disclosure of the commercial registers to the court from an adverse party. According to the TCCP and the TCC, the court can decide on submission of the commercial registers of the parties of the commercial dispute ex officio, or upon request of the parties, even when the parties are foreign real or legal persons.

The disadvantage to a foreign business in resolving disputes in Turkish courts is the potential long-lasting lawsuit process. Foreign real or legal persons who file a lawsuit in Turkey, who participate in a lawsuit that is being examined or who request the enforcement of a foreign court judgment in Turkey, shall pay the security deposit (*cautio judicatum solvi*) determined by the court to cover court costs or enforcement proceedings and the losses of the counter-party. The court may hold the foreign persons exempted from paying this security deposit provided that the reciprocity conditions are fulfilled. On the other hand, there are also some advantages to a foreign business resolving disputes in Turkish courts, such as availability of legal remedies and the possibility of the court's attendance on site. Moreover, referring the case to a Turkish court can be less costly than referring it to arbitration; however, that depends on the value of the asset that is the subject of the case.

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

Yes, an agreement to mediate or arbitrate disputes will be enforced in Turkey. An arbitration agreement shall include the explicit common consent of the parties to submit their dispute to arbitration. Moreover, the arbitration agreement must be in writing. The arbitration agreement must be based on an existing, legal relationship. In this respect, the parties may agree to submit disputes that have arisen, or that may arise, from this relationship.

Depending on the scope of the dispute and the arbitration institution to be chosen, arbitration may cost more for the parties with regard to litigation before state courts. Nevertheless, by referring their disputes to arbitration, the parties may finalise their dispute within a shorter period of time. Arbitration proceedings will also address the confidentiality concerns of the parties, as the proceedings will not be open to the public.

The Turkish legislator considered the UNCITRAL Model Law and Swiss Federal Private Law provisions during the codification of International Arbitration Law No. 4686 (IAL). Therefore, the legislation on international arbitration is compatible with the modern codifications. The IAL is applicable when there is an element of foreignness in the dispute at stake, and when the seat of arbitration is in Turkey or the provisions of the IAL are chosen by the parties or arbitrators.

The parties may also enforce the foreign arbitral awards in Turkey, as Turkey is a member of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention). The enforcement process under the regime of the New York Convention is easier for the parties, as it is prohibited for the courts to examine the merits of the case; that is, the prohibition of the revision au fond. Moreover, the bases for refusal of the recognition and enforcement of an arbitral award are limited under the New York Convention. It is important to note that Turkey opted for two reservations in the New York Convention; namely, the reciprocity and the requirement for the disputes to be of a 'commercial' nature. However, Turkey is an arbitration-friendly country and it takes a positive approach to the enforcement claims under the New York Convention.



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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

A foreign supplier seeking to import and distribute its products in the UAE may do so either by:

- entering into a commercial agency agreement with a UAE national or a company wholly owned by UAE nationals, acting as an agent, and governed by UAE Federal Law No. 18 of 1981 on Commercial Agencies;
- establishing an onshore company for the import and distribution of its products directly in onshore UAE markets;
- entering into a distribution agreement with a UAE entity licensed to import and distribute goods in the UAE. The distribution agreement will be governed by UAE Federal Law No. 5 of 1985 on Civil Transactions;
- entering into a franchising agreements with a UAE entity licensed to import and distribute goods in the UAE. The franchising agreement will be governed by UAE Federal Law No. 5 of 1985 on Civil Transactions; or
- entering into a joint venture agreement with a UAE entity licensed to import and distribute goods in the UAE. The joint venture agreement will be governed by UAE Federal Law No. 5 of 1985 on Civil Transactions.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Where the foreign supplier opts for establishing an onshore company licensed to import and distribute its products in the UAE, the provisions of UAE Federal Law No. 2 of 2015 on Commercial Companies will apply (the Companies Law).

Article 10 of the Companies Law provides that any company established in the UAE shall have one or more UAE partners (either UAE nationals or companies wholly owned by UAE nationals) holding at least 51 per cent of the total capital of the company.

Therefore, up until recently, the position in the UAE was that a foreign investor wishing to establish an onshore company to directly import and distribute goods in the UAE, must partner with a UAE entity, which would be the registered owner of 51 per cent of the company.

It is worth stressing that foreign suppliers cannot transact their trading business in the UAE through a branch. While a branch structure permits a foreign entity to maintain ownership, in practice, the competent licencing authorities do not grant branches of foreign suppliers licences to import and distribute goods in the UAE.

However, UAE Federal Law No. 19 of 2018 on Foreign Direct Investment (the FDI Law) creates a possibility for some foreign investors to set up in onshore UAE without handing over a majority shareholding to a UAE partner.

The FDI Law creates an exemption to article 10 of the Companies Law by allowing up to 100 per cent foreign ownership of companies incorporated in onshore UAE, subject to certain requirements and limited to specific economic activities.

The FDI Law establishes a legal framework for the exemption to the minimum local ownership requirement. It sets out the criteria for companies to be eligible for the exemption, and the procedures they must follow to become exempt.

The main factor determining if a company is eligible and the procedures that apply with respect to the exemption is the economic activity that the company undertakes. The FDI Law creates three categories of economic activities. One category, designated as the 'Negative List', consists of economic sectors that are sensitive domains of the UAE economy and society. Companies that provide activities stated on the Negative List cannot benefit from the FDI Law and must adhere to the minimum local ownership requirements stipulated in the Companies Law.

The second category are companies that provide activities that fall under the 'Positive List'. The UAE Cabinet is set to form a Foreign Direct Invest Committee, which will be tasked with including economic sectors on the Positive List.

It is also expected that the UAE Cabinet will impose conditions and requirements that companies covered by the Positive List must fulfil and adhere to in order to have a greater foreign ownership than 49 per cent.

The third category is made up of economic sectors that do not fall within neither the Negative List nor the Positive List. A competent authority created by the FDI Law will maintain discretion to decide on the application of the FDI Law with respect to companies operating in such sectors.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

Onshore limited liability companies are commonly considered as best suited for an importer owned by a foreign supplier to transact their trading activity in the UAE.

As mentioned under question 3, onshore limited liability companies are governed by the Companies Law. A foreign supplier looking to carry out its trading activity in the UAE through a limited liability company should pay particular regard to the provisions of article 10 of the Companies Law, and the FDI Law, both of which relate to the minimum local ownership requirement in limited liability companies.

To establish as a limited liability company, the company must register a memorandum of association with the competent registrar in the UAE, made in Arabic and attested by a UAE notary public. The memorandum of association is entered into between the shareholders of the company and sets out, among other things, the shareholders' rights, provisions relating to shareholders meetings, duties and powers of directors, and provisions on profit and loss distribution.

Foreign suppliers who must adhere to the 51 per cent local ownership requirement usually enter into 'side agreements' with the UAE partner in addition to the memorandum of association. The purpose of these side agreements is to ensure that the foreign supplier is awarded full control of the onshore limited liability company.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

See questions 2 and 3.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

See questions 2 and 3.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

According to UAE Federal Decree-Law No. 8 of 2017 on Value Added Tax (VAT) (the VAT Law), foreign suppliers established in the UAE must register for VAT if they perform taxable supplies or imports that exceed the mandatory registration threshold of 375,000 dirhams per annum, and they may choose to voluntarily register for VAT if their supplies and imports are less than the mandatory registration threshold but exceed the voluntary registration threshold of 187,500 dirhams.

Additionally, import VAT of 5 per cent is payable in addition to a customs duty of 5 per cent due on movement of goods into the UAE. However, if the importer of record is VAT registered, it is likely that there will be a reverse-charge mechanism available to allow the importer to 'pay' and 'recover' the import VAT at the same time, mitigating any cash flow impact.

Reverse charge is a mechanism under which VAT is required to be paid for goods or services by the recipient instead of the supplier when the supplier is not a resident in the UAE, where the supply takes place. When the reverse charge is applied, the recipient of the goods or services makes the declaration of both their purchase (input VAT) and the supplier's sale (output VAT) in their VAT return. In this way, the two entries cancel each other from a cash payment perspective in the same return.

For the purposes of the VAT Law, 'imports' are defined as goods brought into the UAE from outside the Gulf Cooperation Council area. As a general rule, imported goods are liable to VAT at the point of entry into the UAE. In most cases, a registered taxpayer in the UAE can reclaim the VAT paid on the goods they have imported as input tax. The taxpayer will need the import VAT document to show that import VAT has been paid.

Finally, it is worth stressing that the reverse charge can only be performed by a VAT-registered person. Therefore, cross-border business-to-consumer supplies cannot be subject to the reverse charge.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

As mentioned in question 1, distribution structures available to suppliers in the UAE include the use of:

- distributors, whereby the supplier and the UAE-established distributor enter into a distribution agreement governed by UAE Federal Law No. 5 of 1985 on Civil Transactions;
- franchising agreements and joint venture agreements governed by UAE Federal Law No. 5 of 1985 on Civil Transactions; and
- commercial agencies, whereby the principal and the agent enter into a commercial agency agreement governed by UAE Federal Law No. 18 of 1981 on Commercial Agencies.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

The main laws regulating the relationship between a supplier and its distributor are:

- UAE Federal Law No. 18 of 1981 on Commercial Agencies (as amended by UAE Federal Law No. 14 of 1998, UAE Federal Law No. 13 of 2006 and UAE Federal Law No. 2 of 2010);
- UAE Federal Law No. 2 of 2015 on Commercial Companies; and
- UAE Federal Law No. 5 of 1985 on Civil Transactions.

The government agencies that regulate the relationship between a supplier and its distributor are the Ministry of Economy and the Department of Economic Development in Dubai, Abu Dhabi, Umm al Quwain, Ajman, Fujairah and Ras Al Khaimah.

A consumer protection division exists under each of these departments.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

Termination of a distribution agreement governed by UAE Federal Law No. 5 of 1985 on Civil Transactions

Distribution agreements governed by UAE Federal Law No. 5 of 1985 are subject to the principle of freedom of contract. Accordingly, there are no statutory restrictions on a supplier's right to terminate a distribution relationship without cause where such termination is permitted by the distribution agreement, or when the agreement reaches its contractual term.

Termination of a commercial agency agreement governed by UAE Federal Law No. 18 of 1981 on Commercial Agencies

UAE Federal Law No. 18 of 1981 governing registered commercial agency agreements (the Commercial Agency Law) affords the agent statutory protection against termination of the distribution relationship without cause, or upon such agreement reaching its contractual term. In effect, section 8 of the Commercial Agency Law provides that termination of a commercial agency agreement registered in accordance with the provisions of the Commercial Agency Law is only permitted for a 'material reason'. UAE courts have held that a 'material reason' may include the following:

- the agent's failure to meet sales targets or minimum purchase requirements;
- any breach of the Commercial Agency Law by the agent;
- the agent undertaking activities that compete with the foreign supplier's products or services; and
- the agent failing to maintain the brand and image of the foreign supplier or acting in a manner that damages the reputation of the foreign supplier or its products or services.

Alternatively, the principal and the agent under a commercial agency agreement entered into in accordance with the Commercial Agency Law can mutually agree to terminate their commercial agency relationship following which the agent irrevocably waives its statutory right of protection against termination.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

In the event of a termination without cause of a commercial agency agreement entered into in accordance with UAE Federal Law No. 18 of 1981, the party terminating the agreement faces two material risks with respect to brand visibility and commission.

If the products of an agency agreement are imported by a party other than the registered agent, this agent has the right to request that the UAE customs impound the shipment of these products, and that they block them and prevent them from entering the market. If the products are allowed into the UAE through an entity other than the registered agent, this agent may be entitled to a commission for these sales based on the remuneration agreed in the agreement, and may request that these sales be confiscated. Either party may claim damages if the termination has caused them damages. The agent can also claim compensation for abusive termination under the agreement and damage to reputation, if the principal has not actually performed its duties or collected any commission.

Termination of a distribution agreement regulated by UAE Federal Law No. 5 of 1985 on Civil Transactions is governed by the general principles of contract law, whereby compensation is paid by the breaching party to the innocent party in the event of a breach of contract.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

The UAE allows distribution contracts to include a provision prohibiting such a transfer of the distribution rights. Contracts may include clauses limiting the agent's right to assign their responsibilities to another party; a breach of this provision may constitute a 'material

breach' by the agent that would allow the principal to terminate the agreement. It is also common for contracts to include clauses on the appointment of sub-distributors allowing agents to appoint sub-distributors if the principal has authorised this in writing and whereby the agent shall be fully liable for any compensation to the sub-distributors.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

UAE Federal Law No. 31 of 2006 on Industrial Property, UAE Federal Law No. 5 of 1985 on Civil Transactions, and provisions of competition law all provide regulations on matters relating to confidentiality. However, the absence of a uniform trade secrets law means there is a degree of uncertainty as to protection of these rights under UAE law. UAE courts will generally act to prevent the confidential information of one party being used or disclosed by another party, especially where there are specific contractual provisions in the distribution agreement.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

Restrictions on the distribution of competing products in distribution agreements are always enforceable during the term of the relationship. Most, if not all, such agreements will include a provision stipulating that an agent shall at no time engage in any unfair trade practices with respect to the principal. As for the enforceability of the clause after the term of the relationship, the principal will generally include a clause preventing the agent from distributing competing products for a certain period of time.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

Contracts generally include a resale price maintenance clause whereby a principal and its distributors agree that the distributors will sell the principal's product at certain prices, at or above a price floor (minimum resale price maintenance) or at or below a price ceiling (maximum resale price maintenance). If a distributor refuses to maintain prices, either openly or covertly, the supplier may stop doing business with it.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

Suppliers will generally ensure that the contract contains a clause stipulating that the agent shall comply with the principal's minimum advertised price (MAP) policy, which may be modified or cancelled by the principal. The MAP will generally be appended to the contract.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

A distribution contract may specify that the supplier's price to the distributor will be no higher than its lowest price to other customers.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

A distribution agreement may place restrictions on purchase orders issued to retail accounts. Following these restrictions, the agent must enforce a limitation on purchase by the buyer they deal with, whereby the merchandise purchased by the buyer from the distributor must be sold to the end consumer only. The buyer dealing with the distributor will be expressly prohibited from selling the merchandise purchased to a retailer, or from exporting the items purchased outside the country where the goods were purchased. The buyer will further be required to comply with the supplier's MAP policy.

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

Under a distribution agreement regulated by UAE Federal Law No. 5 of 1985 on Civil Transactions, a supplier may restrict the geographical area to which its distribution partner resells, for example, to a specific territory which can be the country in which the agreement is entered into. The supplier may further restrict the categories of customers to which the distribution partner resells, such as to another dealer who sells similar and competitive products, to any party who may resell the products, or to a customer who the agent has reason to believe will take the product outside the country. Reasonable measures must be taken by the agent to ensure these conditions are complied with.

In relation to commercial agency agreements entered into in accordance with UAE Federal Law No. 18 of 1981, parties are bound to restrict their commercial agency to the territory of the UAE. Accordingly, online distribution under such agreements is restricted by law.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

Under a distribution agreement regulated by UAE Federal Law No. 5 of 1985 on Civil Transactions, the supplier may restrict or prohibit e-commerce sales by its distribution partners, by including a clause in the agreement that states that the distributor must obtain the principal's written consent in order to sell a product on an online platform or through an e-commerce intermediary. The supplier may also prevent the distributor from selling the product to any person or entity who might export the product outside the designated territory.

In relation to commercial agency agreements entered into in accordance with UAE Federal Law No. 18 of 1981, parties are bound to restrict their commercial agency to the territory of the UAE.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

A supplier may restrict the distributor's ability to sell products to any customer that the distributor has reason to believe may export the product outside the designated territory or resell the product on an e-commerce platform, if this has indeed been restricted in the distribution agreement.

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

Under UAE Federal Competition Law (Federal Law No. 4 of 2012), it is prohibited for dominant companies in a relevant market to take advantage of this position to breach, minimise or prohibit competition, by undertaking practices such as price fixing, undercutting prices, discriminating with no objective justification in respect of prices for identical contracts, or obliging a client not to deal with a competitor. Such companies are also prohibited from disseminating false information about products or their prices, and undersupplying or flooding the market with their products.

For the purposes of these provisions, a dominant position arises if the market share of the company exceeds the total transactions in the relevant market. The UAE Cabinet can also, upon recommendation from the Minister of Economy, increase or decrease the rate of this 'economic concentration' depending on economic need.

It is possible for companies to apply to the Ministry of Economy for an exemption from the application of these prohibitions, by adducing evidence to demonstrate that the practice will, in fact, enhance economic development and improve competition.

- 22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?**

UAE Federal Competition Law (Federal Law No. 4 of 2012) prohibits 'restrictive agreements', such as those that specify prices or conditions for the buying or selling of commodities and services, or are tantamount to collusion in respect of tendering and bids, or that have the effect of limiting the flow of commodities and services to the market, or conversely flooding the market with such items. Agreements that divide markets or assign clients based on geographical area, and those that hinder the entrance of businesses to the market, are also banned.

The Competition Law does expressly state, however, that this aspect is subject to the provisions of Federal Law No. 18 of 1981 (as amended) (Commercial Agency Law). Accordingly, registered distribution agreements fall outside the scope of the prohibition on restrictive agreements.

- 23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?**

The effect of registering a commercial agency agreement regulated by UAE Federal Law No. 18 of 1981 (the Commercial Agency Law) with the UAE Ministry of Economy is that the commercial agent has exclusivity for the market.

As per the Commercial Agency Law, third parties are not allowed to import into the UAE any commodity, product, manufactured good, material or any other merchandise that is the subject matter of a commercial agency registered at the Ministry of Economy without the prior consent of the registered commercial agent. Accordingly, only the commercial agent will be able to stop parallel imports that are coming into the UAE through channels other than the registered commercial agency.

- 24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?**

Commonly, under distribution agreements registered in the UAE, the principal and the agent agree that the agent will, in good faith and at its own expense, market, advertise, promote and resell the products to the retailers pursuant to the distribution agreement, consistent with good business practice. The agent will further agree to advertise and market the products it sells in a manner that reflects favourably on the products and the name, goodwill and reputation of the supplier. Finally, advertising and marketing costs can either be shared between the principal and the agent, or solely covered by the agent.

- 25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?**

The supplier may agree with the distributor that the distributor does not acquire ownership of the supplier's intellectual property rights and that these rights remain the exclusive property of the supplier. This may include trademarks and patents. The agreement may also stipulate that if the agent were to acquire intellectual property rights pursuant to the distribution agreement, that these rights would irrevocably be assigned to the supplier, and that the agent would only use these rights to perform its obligations under the distribution agreement.

- 26 What consumer protection laws are relevant to a supplier or distributor?**

Each emirate of the UAE contains a Department of Economic Development that deals with consumer rights issues and manages consumer protection laws. UAE Federal Law No. 24 of 2006 on Consumer Protection provides that anyone offering a product to a customer must comply with health and safety standards (the customer's right to safety), and provide accurate information about the goods (the customer's right to know).

- 27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?**

Products distributed in the UAE must comply with UAE Federal Law No. 24 of 2006 (the Consumer Protection Law) and Cabinet Resolution No. 12 of 2007 Concerning the Executive Regulations of Federal Law No. 24 of 2006.

In summary, the supplier or principal under a distribution agreement or a commercial agency agreement (as the case may be) may be required to recall any product that does not comply with the foregoing statutory provisions concerning consumer protection. However, parties to a commercial agency agreement registered in the UAE Ministry of Economy in accordance with UAE Federal Law No. 18 of 1981 may delineate to the agent the responsibility for carrying out the recall and absorbing the related costs.

- 28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?**

The supplier may warrant that products will be fit for purpose, if operated correctly. It may, however, refuse to warrant that the products will be fit for purpose in all locations or environments, that the products will be error free, and that all errors in the products will be corrected. It may further refuse to warrant that the products will meet the customer's requirements. The agreement may confirm that the distributor will not make any warranties on the supplier's behalf.

- 29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?**

The distribution agreement may include restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products, namely by stating that all data collected on customers and end users shall only be used for the performance of one party's obligations under the agreement. This would indeed prevent the supplier and its distribution partners from exchanging any such information outside the scope of their professional obligations with respect to the agreement.

- 30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?**

Parties to either a distribution agreement governed by UAE Federal Law No. 5 of 1985 on Civil Transactions, or a commercial agency agreement governed by UAE Federal Law No. 18 of 1981 on Commercial Agencies (the Commercial Agency Law), may agree to grant the supplier or principal (as the case may be) the power to approve and revoke the individuals who manage the distributor's or the agent's (as the case may be) business.

However, although the supplier may terminate the distribution relationship if it is not satisfied with the management as agreed in the distribution agreement, termination of the commercial agency agreement will only be possible if breach of the management provisions constitutes a 'material reason' for terminating the commercial agency agreement, in line with the 'agent's protection against termination' encapsulated in section 8 of the Commercial Agency Law.

- 31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?**

There are no circumstances under UAE laws following which a distributor would be treated as an employee of the supplier. Further, the parties to a distribution agreement registered in the UAE commonly agree that the agent, or any director, officer or employee of the agent will be considered as an employee of the supplier. These provisions are intended to exclude the application of UAE labour laws and regulations.

Update and trends

The UAE Cabinet is set to form a Foreign Direct Invest Committee, which will be tasked with determining the economic sectors that will allow for greater foreign ownership for companies operating in such economic sectors.

32 Is the payment of commission to a commercial agent regulated?

Article 1 of Federal Law No. 18 of 1981 defines a commercial agency agreement as an arrangement whereby a foreign company is represented by an agent to distribute, sell, offer or provide goods or services within the UAE against a commission or profit. The payment of a commission to a commercial agent is a condition for the existence of an agency agreement between a principal and an agent. Further, if products are allowed into the UAE through, or services are provided by, another (unregistered) agent, the registered agent will have the right to claim a commission on any profit generated by the sale of these goods or services. The commission will be at the rate stated in the agreement.

33 What good faith and fair dealing requirements apply to distribution relationships?

In distribution relationships, distributors may be restricted from engaging in the following activities with respect to the supplier, product or service:

- engaging in any unfair trade practices;
- making false or misleading statements;
- communicating information with respect to guarantees or warranties to third parties, except as authorised by the supplier; or
- disclosing confidential information.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

Registration of commercial agency agreements governed by UAE Federal Law No. 18 of 1981 on Commercial Agencies

UAE Federal Law No. 18 of 1981 on Commercial Agencies (the Commercial Agency Law) sets out the following requirements for a valid and enforceable commercial agency agreement:

- the agent must be a UAE national or a company wholly owned by UAE nationals (section 2 of the Commercial Agency Law);
- the commercial agency relationship must be exclusive (section 5 of the Commercial Agency Law);
- the commercial agency agreement must be in respect of a defined territory in the UAE (section 5 of the Commercial Agency Law); and
- the commercial agency agreement must be in Arabic, notarised before a notary public, and registered with the UAE Ministry of Economy (section 3 of the Commercial Agency Law).

The effect of registration is that third parties are not allowed to import into the UAE any commodity, product, manufactured good, material or any other merchandise that is the subject matter of a commercial agency registered at the Ministry without the prior consent of the registered commercial agent.

Registration of trademark licence agreements governed by UAE Federal Law No. 37 of 1992 on Trademarks

Trademark licence agreements are governed by UAE Federal Law No. 37 of 1992 on Trademarks (the Trademark Law).

Section 5 of the Trademark Law provides that all trademark licences must be registered with the UAE Ministry of Economy for the licence to be enforceable against third parties.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

The UAE Federal Penal Code (the Code) is the main federal law which regulates anti-bribery practices in the UAE. Articles 234 to 239 of the Code contain provisions that criminalise the bribery or attempted bribery of both public and private sector employees. It applies to the relationships between suppliers and their distribution partners in the UAE.

Under the provisions of the Code, a bribe would be anything that confers a benefit on a public or private sector employee, as the case may be, with the intent to procure that such employee acts in a way that violates the duties assigned to his function or to commit an act that falls outside such duties. Accordingly, it is important for parties under a distribution agreement to have regard to the foregoing provisions of the Code.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

There are no limitations under UAE law on the enforceability of distribution agreements or commercial agency agreements validly entered into in accordance with the provisions of UAE Federal Law No. 5 of 1985 on Civil Transactions (with respect to distribution agreements) or UAE Federal Law No. 18 of 1981 on Commercial Agencies (with respect to commercial agency agreements).

In relation to mandatory provisions, see in question 34.

Finally, there is a 'duty to act in good faith' implied by section 246 of UAE Federal Law No. 5 of 1985 on Civil Transactions into all agreements and contracts that requires the parties to act with 'utmost good faith' when performing their contractual obligations. The implied duty to act in good faith applies to distribution agreements and commercial agency agreements.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

Distribution agreements governed by UAE Federal Law No. 5 of 1985 are subject to the principle of freedom of contract. Accordingly, there are no statutory restrictions on the parties' choice of law and jurisdiction to govern their distribution relationship.

However, in relation to commercial agency agreements entered into in accordance with UAE Federal Law No. 18 of 1981, parties are bound to submit their contractual relations to the jurisdiction of UAE federal courts, which will apply UAE federal law.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

See question 37.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

In proceedings before UAE courts, a party's (or third party to the claim) duty to disclose (and allow inspection) arises only if and when the court makes an order for specific disclosure. It is worth noting that UAE courts have seldom made orders for such disclosure.

Moreover, the following are interim remedies available to litigants before an UAE onshore court:

- application for summary judgment;
- interim injunctions; and
- interim cost orders.

Security for costs orders – made pursuant to a defendant's application, if it is concerned that the claimant does not have sufficient funds to meet the costs of the proceedings if the action is successfully defended – are not available under UAE civil procedure rules.

Finally, the general principle under UAE civil procedure rules is that the unsuccessful party will be ordered to pay the costs of the successful party. However, in practice, an award of costs in the UAE is usually restricted to litigation disbursements such as court fees and expert fees. Only rarely have parties to a dispute been able to recover the fees of their legal representatives in full.

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

An agreement to mediate or arbitrate disputes will only be enforced in the UAE if it relates to a distribution agreement regulated by UAE Federal Law No. 5 of 1985 on Civil Transactions. As such agreement is subject to the principle of freedom of contract, there are no statutory limitations on the terms of agreement to arbitrate set out under it.

However, an agreement to arbitrate or mediate under commercial agency agreements entered into in accordance with UAE Federal Law No. 18 of 1981 on Commercial Agencies will not be enforceable, as contractual relations and disputes arising from such agreements are subject to the exclusive jurisdiction of UAE federal courts (which will apply UAE federal law).



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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

A foreign company can conduct business in the United Kingdom without setting up a legal entity, thus avoiding most UK company law requirements. If setting up a permanent place of business in the UK to directly carry out business, it must register as a branch office of an overseas company and register its constitution together with a statement of the power of its directors to bind the company.

Another option is to incorporate a subsidiary company in the United Kingdom. The principal advantage over a branch office is that, because UK courts assiduously enforce the doctrine of corporate personality, the main overseas business can, in most cases, be shielded from the risks incurred by the UK business.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Yes, there are currently few restrictions on foreign ownership of UK companies. After Brexit, freedom of establishment for EU companies may fall away, so companies should review the impact on their structure. In certain limited situations in regulated industries such as financial services, the controllers of a company must be approved by the regulator. The UK government may also seek to intervene if a business is in a sensitive defence sector. However, there are new regulations which have increased the level of scrutiny of certain types of foreign investments (see question 4).

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

Several forms of corporate vehicle can be registered in the UK that are suitable for an importer owned by a foreign supplier. Which is most suitable will depend on a range of factors largely to do with the requirements of the markets the entity serves, as well as the tax treatment of the entity in the UK and foreign jurisdiction. These include a UK limited company, a UK branch and partnerships (limited liability partnerships, limited partnerships and general partnerships).

The method of formation will depend on the type of entity. See above for branches and UK establishments (see question 1). Limited liability companies and limited liability partnerships must be incorporated and registered with Companies House. Limited partnerships are generally set up by contract and must be registered at Companies House. General partnerships are created by agreement or simply by entering into a relationship in common with a view to profit (there need not be an underlying written contract for a partnership to be created). The primary statutory legislation that applies is the Companies Act 2006, the Limited Liability Partnership Act 2000, the Limited Partnership Act 1907 and the Partnership Act 1890 respectively.

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

No single piece of legislation regulates foreign investment in the United Kingdom. There is no general requirement for foreign investment in the UK to be registered. The Industry Act 1975, section 13, allows the

government to intervene in relation to a change of control of 'an important manufacturing undertaking' contrary to the interests of the UK. This does not appear to have been acted upon to date. As a result of the Enterprise Act 2002 (Turnover Test) (Amendment) Order 2018 (Turnover Test Order 2018), which came into effect from 11 June 2018, the UK's merger control system has been tightened to allow increased scrutiny of the national security implications of particular investments. This Order applies to investments in the defence, dual use, quantum tech and CPU sectors, and reduces the threshold for triggering a relevant merger situation (and may result in an investigation by the UK Competition and Markets Authority) in respect of smaller companies than usual. Additionally, the Enterprise Act 2002 (Share of Supply Test) (Amendment) Order 2018 (Supply Test Order 2018), which also came into effect from 11 June 2018, provides that the acquisition of a company in one of the above sectors (with a 25 per cent share of supply of goods or services in the UK pre-merger) will also trigger a relevant merger situation. The European Union is also consulting on proposals on foreign investment screening but these are unlikely to be in force before the UK exits the EU, likely to be after March 2019, subject to a transitional period likely to last until the end of 2020. The UK government is also intending to introduce a further national security vetting arrangement to protect the security of certain infrastructure where there are certain triggering events.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

Yes, subject to the usual competition law concerns.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

The UK tax system broadly applies equally to foreign suppliers and UK suppliers operating in the United Kingdom. Profits from a UK limited company and a UK branch of a foreign supplier forming a UK permanent establishment are taxed similarly, and will generally be liable to UK corporation tax. Partnerships (including LLPs) carrying on business in the UK will generally be tax transparent, meaning that the partners will be taxed on their own share of the profits. Often the tax treatment of the UK entity in the relevant foreign jurisdiction, and whether tax transparency is desirable, will influence the more suitable entity in each case.

The UK tax considerations depend on the activities carried on in the UK. If the entity employs individuals then it is likely that it will be obliged to deduct income tax and employees' national insurance contributions from payments made under the UK's pay-as-you-earn system, and remit the tax deducted together with employer's national insurance contributions (another form of tax) to HM Revenue & Customs. Furthermore, the business should consider whether it is obliged, or whether it may be desirable, to register (and account) for value added tax, and whether it is required to account for customs duties.

The UK tax system typically requires resident companies to withhold tax in relation to the payment of interest or royalties to non-resident recipients (corporate or individuals) at a rate of 20 per cent. However, the UK is party to a large number of double tax treaties with

other countries which remove or reduce the withholding tax rate for payments to recipients in the relevant jurisdiction.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

Any number of structures can be chosen depending on commercial, market and tax considerations. Normally, some form of market representative, whether employed or otherwise contracted, would be sensible. An agent with varying levels of authority or indeed a stock-holding distributor with obligations to expand sales might be attractive. Depending on the strength of the marketing format, franchising could be an attractive option to expand. Supply chain efficiency and relationships down the chain will dictate what is the most appropriate model to pursue. Typically, from a legal and commercial perspective, the following are common relationship characteristics:

- exclusive: appointment of one distributor for the territory or a particular customer group and the supplier is prevented from appointing another distributor or selling into the territory or customer group directly;
- sole: appointment of one distributor for the territory or customer group and the supplier is prevented from appointing another distributor for the territory or customer group but the supplier retains the right to sell into the territory;
- non-exclusive: no restrictions on the supplier allocating distribution rights to more than one party for a particular territory or customer group or supplying directly; and
- selective: only approved dealers are entitled to handle and resell the goods, and restraints can, in certain circumstances, be imposed on other resellers. Any distributor fulfilling a set of objective, transparent and non-discriminatory criteria, normally based on quality, is admitted to the distribution network. Selective distribution is typically used for high-end or prestige goods.

In contrast, a commercial agent or sales representative is an agent of the seller. The agent acts on behalf of the principal under power of attorney and does not have a direct contract for supply with the customer and will normally not bear any financial risk. An agent enters into the supply agreements in the name and for the benefit of the foreign supplier and receives a commission (typically a percentage of the price) as payment. Using an agent has the advantage that the supplier can set the price at which the products are sold to the customer. This is not permitted with a distributor. The main disadvantage of using an agent is that they are entitled to statutory compensation upon termination. An agent's activities can be limited to introducing customers and contracts to the principal (marketing agent) or they can be sales agents, where the agent has authority to conclude contracts with customers on behalf of their principal. As with distribution agreements, agency agreements can be exclusive, sole or non-exclusive.

The supplier may opt for a franchising format for distribution of goods and services under the franchisor's business model and brand with associated know-how or methods. There is no UK regulation of franchising and so general law and legal principles apply. The British Franchise Association requires its members to abide by the European Code for Franchising but compliance cannot be guaranteed.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

There are no specific UK laws relating to distribution that govern the relationship between a supplier and its distributor. Common law principles of contract will apply to any agreement between the parties, as will certain general statutory provisions in regulated sectors such as financial services.

There are specific rules governing agency relationships where an agent is a 'commercial agent' as defined in the Commercial Agents (Council Directive) Regulations 1993 as amended (Agency Regulations). Those Regulations are based on EU law but they are expected to remain post Brexit. The Regulations apply where an agent is a self-employed intermediary who has the authority to negotiate the sale or purchase of goods on behalf of or in the name of a principal,

regardless of whether the agent and supplier have a written agreement. Computer software amounts to 'goods' for the purposes of the Regulations (*Software Incubator Ltd v Computer Associates Ltd* [2016] EWHC 1587 (QB); Official Transcript; QBD (Merc) (London); 1 July 2016). There are certain exclusions from the Agency Regulations such as where the agent is involved in the sale and purchase of services rather than goods, or where the agent operates on commodity exchanges or markets (*W Nagel (A Firm) v Pluczenik Diamond Co NV* [2017] EWHC 2104 (Comm), 11 August 2017). The scope and application of these agency rules differ a little between member states of the European Economic Area (EEA), as does the approach of their respective courts.

General statutory rules that may be relevant to both distribution and agency relationships include (but are not limited to):

- Competition law – (i) Chapter I of the Competition Act 1998, which follows European competition rules on vertical distribution agreements, and (ii) Chapter II of the Competition Act 1998, which prohibits the abuse of a dominant position. These rules impose limits on the restrictions that a supplier can impose on a distributor or agent or vice versa.
- The Bribery Act 2010 – under section 7 of that Act, a commercial organisation will be guilty of an offence if a person associated with it bribes or attempts to bribe another person for the commercial organisation's commercial advantage. A person is 'associated' with a commercial organisation for these purposes if that person performs services on behalf of the commercial organisation, including agents and, potentially, distributors performing services on behalf of the supplier. The European Court of Justice (ECJ) has, in another context, ruled that a distributor provides services for its supplier (*Corman-Collins SA v La Maison du Whisky SA* (C-9/12)). See question 35. The same would apply to an agent.
- The Modern Slavery Act 2015 – in force since October 2015, this legislation requires certain commercial organisations to publish a slavery and human trafficking statement every financial year outlining the steps taken to ensure that slavery and human trafficking are not taking place in the business or anywhere in its supply chains. Organisations are caught if they carry on business (or part of a business) in the UK and have turnover above £36 million. While the statutory obligation is easily satisfied – publish a statement as to what the entity has done – it is increasingly a requirement of retailers and others demanding a system of compliance and verification that no slavery or exploitation is in a supplier's supply chain.
- The Unfair Contract Terms Act 1977 (UCTA) – the UCTA applies in B2B contracts mainly to unfair terms that have the effect of restricting or excluding a party's liability. Certain contracts, such as international supply contracts, are excluded from the application of the UCTA.
- The Data Protection Act 2018, the General Data Protection Regulation (Regulation (EU) 2016/679) (GDPR) and Privacy and Electronic Communication Regulations – these have an impact on the relationship between the parties as to how they may share and deal with customer and end-user data. The effects of this are further discussed in question 29.
- The Reporting on Payment Practices and Performance Regulations 2017 – these require large companies and large LLPs which exceed certain size criteria to report on a half-yearly basis on their payment practices, policies and performance for financial years beginning on or after 6 April 2017.

There is no government agency that specifically regulates the relationship between distributors or agents and suppliers. In practice, there are several agencies with which a supplier or distributor may have to deal.

The Competition and Markets Authority (CMA) is the primary competition authority in the UK and is responsible for ensuring that businesses comply with the competition laws. Sectoral regulators, such as the Financial Conduct Authority in the financial services sector, have certain competition powers exercised concurrently with the CMA.

Other bodies, such as Trading Standards, the Advertising Standards Authority, the Food Standards Agency and HM Revenue and Customs may also be relevant. There might also be other sector-specific agencies (eg, in the pharmaceutical sector, the Medical and Healthcare Products Regulatory Agency) that also have a bearing on distribution relationships.

In terms of supply to major supermarkets, the Groceries Code Adjudicator administers a code, the Groceries Supply Code of Practice (GSCOP), governing the relationship between the largest UK supermarkets and their direct suppliers to reduce or eliminate unfair or unreasonable treatment. This deals with behaviour that transfers undue risk to suppliers such as direct or indirect delays to payment, changes in supply terms, charging for prime positioning or increased shelf space unless connected with promotions and a number of other practices found to be unfair. Its remit is limited to direct suppliers to supermarkets and not to the indirect supplier.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

No, if the provisions on termination without cause are clear and unambiguous, the UK courts will uphold freedom of contract. It should be borne in mind that there are three legal jurisdictions in the UK. England and Wales is the largest jurisdiction and most contracts are under English law and subject to the English court system. The Scottish courts are largely independent and, while commercial law is often identical or similar, there are some differences. The courts in Northern Ireland apply very similar legal principles to those in England and Wales.

Where the agreement makes no specific provision for termination without cause or there is no written agreement in place, it can be terminated provided reasonable notice has been given to the other party. What constitutes reasonable notice is assessed at the time of breach, taking into account various factors. The key is the impact on the party to whom notice is given. The courts have considered this issue on numerous occasions and the following are the sorts of factors which they have taken into account:

- the formality of relationship;
- the availability of an alternative supplier;
- the state of affairs at termination (eg, promotion spend);
- the time required to wind down the business;
- the percentage of turnover the contract represents;
- market practice for termination in the relevant industry;
- the notice period specified for termination for cause;
- the likelihood of redundancies occurring;
- the potentially damaging effect of rapid termination; and
- the length of the parties' relationship (although frequently this is not a relevant factor).

One of the most important factors which the courts will take into account is the percentage of the supplier's turnover that the contract represents. If this is a high percentage, it follows that a longer notice period may be required.

It is important that a party serving notice gives some consideration to the sort of issues and factors listed above, as this will help to demonstrate that it has been reasonable in serving notice. In one case, the courts suggested that nine months would be a reasonable notice period in a case where the relationship lasted two-and-a-half years, the distributor had invested heavily and it would take time to find an alternative brand to represent. In contrast to certain other types of contracts, the court suggested that a longer period of notice may be due in the early years of a distribution relationship given the heavy investment in those years by the distributor and where the return is obtained only once the customer base is established (*Jackson Distribution Limited v Tum Yeto Inc* [2009] EWHC 982 (QB)). (See also *Hamsard 3147 Limited (trading as 'Mini Mode Childrenswear') v JS Childrenswear Limited (In Liquidation) and Boots UK Limited* [2013] EWHC 3251 (Pat)). The 'correct' period of notice, however, depends very much on the facts of each case.

Where a supplier decides not to renew a contract, it will expire at the end of the relevant term. If performance of both parties continues beyond the end of the contractual term, a contract by conduct will be formed, which is terminable on reasonable notice.

Grocery retailers governed by the GSCOP – currently the 10 largest grocery retailers in the UK based on turnover above £1 billion – are also specifically required to give reasonable notice if they intend to cease to purchase groceries for resale from a supplier or significantly to reduce the volume of purchases made from that supplier. The definition of

supplier for the purposes of GSCOP includes any person carrying on (or actively seeking to carry on) a business in the direct supply to any retailer of groceries for resale in the United Kingdom.

In an agency relationship where the Agency Regulations apply, minimum notice periods must be given by a principal to terminate an agent's contract. This is linked to the length of the relationship until termination. The minimum notice period is one month in the first year of the relationship, two months in the second year and three months in the third year and any subsequent years. It is open to the parties to agree longer periods.

A principal is entitled to decide not to extend or renew an agency that has been concluded for a fixed period or that is due to terminate at the end of its term.

Recent case law has suggested that there may be an implied term in certain categories of contract that parties to a contract must act in good faith when terminating a contract (see question 33).

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

Distribution

If termination complies with the express terms of the agreement (eg, the agreement provides for termination without cause on notice), no mandatory compensation or indemnity will be payable unless provided for in the agreement. The other party will have no other remedy for termination of the agreement in these circumstances.

If the agreement is silent on the circumstances in which the agreement can be terminated, common law implies that the agreement can be terminated only upon reasonable notice (see question 9) or in cases of repudiatory breach.

If the agreement is terminated in breach of the express or implied terms of the agreement or, in the absence of written notice provisions, reasonable notice of termination is not given, no mandatory compensation or indemnity is payable but the distributor may be entitled to damages for breach of contract. Where Scots law applies, the courts may prefer to enforce performance if not validly terminated.

Agency

In an agency relationship to which the Agency Regulations apply, the Agency Regulations provide that an agent is entitled to compensation or an indemnity for termination in certain circumstances. This is in addition to damages for breach of contract. Where a UK law applies, the parties can make an express choice in their agreement for either indemnity or compensation to apply. If an indemnity is not expressly provided for, the default concept applicable will be compensation – UK law defaults to compensation in the absence of a choice of indemnity or indeed in the absence of any choice at all. In *Shearman v Hunter Boot* [2014] EWHC 47 (QB), it was held that a clause that provided the agent was entitled to either compensation or indemnity, whichever concept produced the lower sum, was invalid. The agent was held to be entitled to compensation. In a subsequent case, a similar provision in an agreement that provided for indemnity, but compensation if cheaper, was allowed to be excised as unenforceable, leaving indemnity as the available award (*Brand Studio Ltd v St John Knits, Inc* [2015] EWHC 3134 (QB)). In *Hunter Boot*, the principal failed to argue that the clause should be severed, so as to leave the indemnity provision intact.

It is not possible for the parties to exclude the right to indemnity or compensation in the contract. Indemnity is capped (at one year's commission) and is due only to the extent that the agent has brought in new customers or significantly increased the principal's business with existing customers and substantial benefits continue to be derived by the principal from those customers. Compensation is calculated to be equivalent to the value of the agency business, including goodwill, at termination (*Lonsdale (t/a Lonsdale Agencies) v Howard & Hallam Limited* [2007] UKHL 32). This is based on the legal assumption there is a 'hypothetical purchaser' of the agency.

The Court of Appeal decision in *Warren (T/A On-Line Cartons and Print) v Drukkerij Flach BV* [2014] EWCA Civ 993, provided further guidance on what the valuer should assume when valuing the agency business. The principal terminated the agency agreement and a dispute arose about how much compensation was due to the agent under Regulation 17. At first instance, the judge assumed, first, that there was a hypothetical purchaser who was able to purchase the agency business. This assumption was correct and followed the rule in *Lonsdale*.

However, the judge also assumed that the hypothetical purchaser would have been prepared to pay an actual price for the business and noted that his function was to determine that price. That part of the judgment was overruled by the Court of Appeal; it was quite possible that a hypothetical purchaser would not have been prepared to pay any price for the agency business, for example, where an agency business was terminally in decline. Where a supplier terminates a successful and profitable agency business compensation figures can be substantial. Legal advice should be taken before taking this step.

The right to compensation or indemnity will be lost when the principal terminates with cause in circumstances where immediate termination would be justified or where the agent terminates the agreement (unless the agent does so in circumstances attributable to the principal (unreasonable conduct) or where it is unreasonable to require the agent to continue the agency owing to infirmity, age or illness).

Grounds that would justify immediate termination by the principal are likely to be similar to fundamental or material breach of contract but the English court has held that gross personal abuse of the worst kind in two telephone calls was enough (*Stephen Gledhill v Bentley Designs (UK) Ltd* [2010] EWHC 1965 (QB)). In another case, publication of disparaging remarks by an agent and its employees of its principal (meaning its poor services) was not grounds to justify immediate termination and denied compensation. The breach was not a breach of condition (ie, in English law a term of the contract serious enough to justify repudiation of the contract) (*Crocs Europe BV v Craig Lee Anderson t/a Spectrum Agencies* [2012] EWCA Civ 1400).

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

Parties are generally free to contract on the terms as they wish. The UK courts are likely to enforce a clause prohibiting the transfer of the distribution rights to the supplier's products to a third party. What is more commonplace, however, is that such a transfer would be subject to the supplier's consent.

A provision prohibiting a change in ownership of the distributor or the transfer of its business to a third party is less common. A more common approach is for the supplier to have a termination right in the event of a change of control or transfer of business of the distributor that it does not consent to.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

Confidentiality clauses in distribution and agency agreements are common and will generally be enforceable. However, it is sensible to restrict such clauses to what is reasonably required to protect confidential information, having regard to the geographical and product scope of the distribution agreement and duration. Depending on how they are drafted, confidentiality provisions have the potential to restrict competition contrary to article 101(1) of the Treaty on the Functioning of the European Union (TFEU) or Chapter 1 of the Competition Act 1998. This would render such clauses void and unenforceable unless an exemption is available under the Vertical Restraints Block Exemption Regulation (VRBE) (ie, the supplier and the distributor each have a market share below 30 per cent on any of the relevant markets affected by the agreement).

For example, *Jones v Ricoh UK Limited* [2010] EWHC 1743 (Ch) concerned a confidentiality agreement put in place between CMP (Jones) and Ricoh. CMP helped corporate customers purchase their photocopying and other requirements and CMP did not want Ricoh to cut them out by forging a direct relationship with the clients (which it needed to disclose to Ricoh during the course of their trading relationship). The agreement restricted Ricoh from using this customer information to trade directly with them. The clause prevented Ricoh and its 150 group companies from making or accepting any approach to or from any contact with any client of CMP, any governmental body or regulatory or other authority or any other person who to Ricoh's knowledge 'has any prospective connection' with CMP. When Ricoh had bid for a contract

with one of CMP's clients, successfully, CMP sued Ricoh for breaching the confidentiality agreement.

The court held that the wide scope of the clause breached article 101 TFEU as it had both an anticompetitive object and effect. It went further than was necessary to protect CMP's confidential information. The clause had a very broad reach, was unlimited in place, of uncertain and extensive ambit in time, and applied to dealings by Ricoh and its associated companies that were not only plausible, but very likely to occur. Where any confidential information was still with Ricoh, it prevented 150 of its group companies from making approaches. Although CMP argued that the clause benefited from an exemption under the VRBE, the court found that, for the purposes of the confidentiality agreement, the parties were not acting at different levels of trade (a prerequisite for the application of the VRBE).

Confidentiality agreements or clauses between undertakings clearly operating at different levels of trade, such as suppliers, distributors or agents, are likely to have a greater chance of benefiting from the exemption available under the VRBE.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

This is an issue governed by principles of EU competition law and likely to be similar in all states within the European Union and EEA. Post Brexit, UK law may begin to diverge. Non-compete obligations are dealt with under the VRBE and to the extent they comply with its conditions, will be enforceable.

For the purposes of the VRBE, a 'non-compete obligation' includes any direct or indirect obligation causing the buyer not to manufacture, purchase, sell or resell goods or services; as well as any direct or indirect obligation on the buyer to purchase from the supplier or someone designated by the supplier more than 80 per cent of the buyer's total requirements of that product or its substitutes. To benefit from the protection of the VRBE and ensure enforceability, the non-compete should not exceed five years' duration or be indefinite (an obligation that is automatically renewable is regarded as indefinite). A longer duration is permissible only where the contract goods or services are sold by the buyer from premises and land owned by the supplier or leased by the supplier from third parties. In those circumstances, the duration of the non-compete should not exceed the period of occupancy of the premises by the distributor. The exemption cannot be relied upon to exempt an agreement between competing undertakings, unless one of them has turnover below €100m except where the appointment is non-reciprocal and the supplier is both a manufacturer and a supplier of goods but the buyer is only a supplier, not a manufacturer or where the supplier provides services at several levels of trade and the buyer is at the retail level and is not a competing undertaking at the level at which it purchases.

A post-term non-compete obligation will not benefit from the VRBE unless:

- it is limited to goods or services that compete with the contract goods or services;
- it is limited to the premises and land from which the buyer has operated during the contract period;
- it is indispensable to protect know-how transferred by the supplier to the buyer; and
- it is limited to a period of one year after termination of the agreement.

This is without prejudice to the possibility of imposing a post-termination restriction which is unlimited time on the use and disclosure of know-how which has not entered the public domain.

Restrictions in agreements that are de minimis or essential for the protection of the reputation and identity of the brand or network are not caught.

In selective distribution, resellers can be prohibited from selling competing products in general, as long as the duration of that obligation is not capable of exceeding five years and the obligation is not targeted so as to exclude 'particular competing suppliers'.

Clauses that are not automatically given protection and enforceability by the VRBE would have to be individually assessed under article 101(3) TFEU to determine whether on their facts they merit being exempted and unenforceable (and therefore their position is much more uncertain).

In an agency relationship, preventing an agent from acting for a competing principal is commonly dealt with in the agreement but, if not, it may be implied either from correspondence or from the agent's obligation to act 'dutifully and in good faith' under Regulation 3 of the Agency Regulations, and in accordance with the other general fiduciary responsibilities of an agent at common law. However, that will be affected by knowledge and delay or acquiescence on the part of the principal. In *Rossetti Marketing v Diamond Sofa Co Limited* [2012] EWCA Civ 1021, the court initially ruled that the fact the agent had an agency selling competing goods was not a fundamental breach of contract so the agent was still entitled to compensation when the principal terminated that agency. The judge noted that the principal had known for some time that the agent had a competing agency selling sofas for a competing brand.

The principal appealed this to the Court of Appeal, which looked more closely at exactly what the principal knew about the agent's other agency and when. It came to the opposite conclusion, ruling that the principal had not initially understood that the agent would be selling goods that were directly competing with his own. Therefore, the principal could not be held to have consented and selling directly competing goods was, in this instance, held to be a fundamental breach of contract.

Principals should bear in mind that requiring an agent to take on a product that competes or conflicts with other products handled for other principals may entitle the agent to terminate and claim compensation or indemnity. Restrictions on agents selling competing products may also infringe competition law in certain circumstances if the non-compete obligations have significant foreclosure effects on a relevant market.

After termination of an agreement to which the Commercial Agents (Council Directive) Regulations 1993 apply, a restraint can be imposed on an agent handling competing products but subject to a maximum of two years.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

Distribution

In distribution arrangements, competition law requires that a supplier does not dictate the prices at which its distribution partner resells its products, whether directly or indirectly (known as resale price maintenance or RPM). RPM is classified as a hardcore infringement and, as such, it is irrelevant that the parties have low market shares or are otherwise insignificant in market terms.

Online markets and competition (and other issues for consumers) are a major area of focus for the UK CMA and, in particular, tackling RPM and online minimum advertised pricing restraints that create price floors. It is difficult (though conceivably possible) to justify these practices on efficiency grounds (eg, to prevent free riding, improve customer service or protect brand image) under article 101 TFEU.

Recommended or maximum sales prices (but not minimum prices) are acceptable but should be analysed carefully to ensure they do not, in effect, constitute indirect resale price maintenance. Other forms of indirect resale price maintenance include:

- fixing maximum discounts from prescribed prices;
- making supplier rebates and reimbursement of promotional costs subject to downstream pricing level;
- linking price to competitors' resale prices; and
- threats, intimidation, warnings, penalties, delay or suspension of deliveries or contract terminations.

A ban on supplying discounting outlets would be regarded as interference in pricing policy except where the ban was imposed in the context of protecting the allure and prestigious image of a brand or mark in a selective distribution system (which bestows on the goods an aura of luxury) and the discounting involved a breach of a trademark licence (*Copad SA v Christian Dior*, Case C-59/08). Suppliers operating selective distribution systems may also be able to restrict authorised retailers from using third party online marketplaces (see question 19).

The VRBE Guidelines of the European Commission suggest an efficiency defence is available in the following very limited circumstances in relation to RPM that is used:

- during the introductory period of expanding demand;
- for a coordinated short-term low-price campaign (two to six weeks) in a franchise system; or

- in relation to complex or experience products, the extra margin would allow distributors to provide additional pre-sales services where free-riding is a problem.

There has been an upturn in enforcement of RPM at UK and EU level in recent years.

In 2013, the CMA issued infringement decisions against mobility scooter suppliers for bans imposed on online sales and online advertising of prices below a recommended resale price even where actual prices in the showroom were unrestrained. Such a practice reduces transparency and increases search costs. The fact that these restraints were imposed in the sale of mobility scooters for less mobile individuals heightened their impact – web searches being all the more important for those who would find it challenging to visit bricks and mortar outlets. In May 2017, the CMA imposed substantial fines on suppliers in the light fittings sectors, finding that they had illegally engaged in online resale price maintenance with some of their retailers in specifying the minimum prices that the retailers could advertise for sales of the suppliers' products over the internet (see question 15).

In a first for UK competition enforcement, in 2016, the CMA also fined a supplier of posters, Trod Limited, for agreeing with a competing supplier that they would not undercut each other on Amazon Marketplace. Automated pricing software was used to implement this agreement.

The European Commission issued fines exceeding €111 million (in July 2018) to four consumer electronics manufacturers for restricting their online retailers from setting their own retail prices. These restrictions were enforced by way of threats or sanctions, such as blocking of supplies. Pricing algorithms were used that automatically adapted retail prices to those of competitors, and sophisticated monitoring tools allowed the manufacturers to effectively track resale price setting in the distribution network and to intervene swiftly in case of price decreases. The European Commission opened an investigation following its e-commerce sector inquiry. RPM remains an enforcement focus for the European Commission.

Agency

In agency relationships, the principal can retain complete control over the price at which its agent resells its products provided the agency relationship is regarded as 'genuine agency'. The determining factor is the financial or commercial risk borne by the agent in relation to the contract activities: those directly related to the contracts entered into by the agent for the principal; and those associated with investment for entry to the market – usually 'sunk' costs. When the agent bears no such risks, or insignificant risks, its activities are not economically distinct from the principal's, and article 101 TFEU does not apply. If an agency agreement lies outside article 101 TFEU, all clauses that are an inherent part of the agency agreement are free from scrutiny. The principal may legitimately restrict the customers to whom, or the territory in which, the agent sells the goods, and also dictate the price and conditions for sale through the agent. If an agent cannot be regarded as a 'genuine agent', it must be permitted to use its commission to offer discounts to customers. It is often unclear whether platforms or online portals should be regarded as true agents. Agency agreements have been considered in a number of cases involving digital platforms, but the authorities have shied away from concluding on the issue.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

A supplier is entitled to suggest resale prices (commonly referred to as recommended resale prices or RRP) but should avoid applying any incentives or pressure to abide by those RRP as this would be likely to be viewed as indirect RPM. The UK's competition authority has taken action against agreements not to advertise discounted prices.

The CMA fined a supplier of light fittings (National Lighting Company Group) for a minimum advertised pricing policy that restricted the price at which retailers could sell the supplier's products online. In the CMA's view, these arrangements restricted the retailers' ability to sell their products online at independently determined prices, reducing price competition between competing retailers and contributing to keeping prices artificially high.

The CMA has previously concluded that the application of a minimum advertised price (MAP) policy genuinely restricted in practice the ability of resellers to determine their online sales prices at a price below the MAP, and therefore amounted to RPM in respect of online sales of the product (see, for example, commercial catering equipment sector: investigation into anticompetitive practices). The European Commission would likely adopt similar reasoning and consider minimum advertised pricing policies as an indirect means of RPM that do not benefit from the VRBE.

Unilateral minimum retail pricing policies are not accepted. Announcing a minimum resale price and refusing to supply those distributors that did not observe it (as per the US *Colgate* doctrine) would probably be regarded as indirect RPM and involving consensus or acquiescence.

There are other ways in which a supplier can attempt to influence pricing, which fall short of RPM. For example, it can oblige distributors to follow its instructions with regard to advertising, provided that those instructions do not seek to regulate the advertising of prices or conditions of sale. This does not prevent a supplier from encouraging the distributor to achieve optimum brand positioning, provided there are no incentives offered or pressure applied to price at, or above, a notified recommended resale price.

A supplier may set a maximum resale price provided it does not, in effect, mean a fixed resale price.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

The prevalence of retail most-favoured-nation (MFN) clauses in the context of online platforms such as online travel agents, price comparison websites (PCWs) and online marketplaces, such as Amazon marketplace, iBookstore, Booking.com, Expedia and so on, has been highlighted by recent competition investigations across the European Union. When adopted by such platforms in their agreements with the providers or sellers seeking to reach consumers through the platforms, MFN clauses can ensure that the provider or seller does not charge a higher price on their platform than it does when selling directly, on another platform or via another channel.

In the UK, the competition authorities considered online hotel booking sites and their restraint on a hotel group offering room-only rates at prices lower than the rates offered by the price comparison sites. Initially, the UK authorities accepted commitments from the hotel group, IHG, from Booking.com and Expedia that allowed this hotel group to offer discounts to a closed group of members. This was successfully challenged by a metasearch site, Skyscanner Ltd, on process grounds and eventually the competition authority closed the file without determining whether the MFN was lawful.

In its investigation into the UK private motor insurance sector, the CMA drew a distinction between the use of what it termed narrow and wide MFNs in agreements between private motor insurance providers and PCWs. Although it recognised that MFNs on PCWs may result in efficiencies (such as reducing search costs for customers), the CMA concluded that widely drafted MFNs were not necessary to achieve those benefits. Therefore, it found that narrow MFNs, which require that the price on the insurer's own website is no cheaper than that offered to the PCW, were acceptable. Wide MFNs, which ensure the price offered to the PCW is no higher than the price offered directly or via any other channel, were prohibited by means of an order applicable in respect of significant PCWs (the Private Motor Insurance Market Investigation Order 2015).

However, there is still much uncertainty with different approaches being taken in EU jurisdictions. The German competition authorities came down against narrow MFNs in the *Booking.com* case, whereas other national competition authorities have accepted commitments permitting narrow MFNs. Elsewhere in Europe, notably France, Italy, Austria and Switzerland, moves were made in 2017 to legislate to ban price parity clauses.

In 2016, the CMA sent a questionnaire to a large sample of hotels in the UK as part of a joint monitoring project, in partnership with the European Commission and nine other competition agencies in the EU. This project is looking at how changes to hotel room pricing terms, and other recent developments, have affected the market, in particular, whether the Europe-wide removal by online travel agents Expedia and

Booking.com of certain 'rate parity' or 'most-favoured-nation' clauses in their standard contracts with hotels in July 2015 has affected the market. The European Commission and 10 national competition authorities published a report in 2017 on the use of such price parity clauses in the hotel booking sector which indicated that the improvements made by online travel agents 'go in the right direction'. The CMA subsequently announced in October 2017 that it was opening an investigation under its consumer law powers into hotel booking websites to determine whether consumers were able to get the best deal. It launched enforcement action in June 2018 to ensure booking sites complied with the law.

The CMA also looked at MFNs in the context of online auction services in 2017 that concluded after the CMA accepted undertakings from ATG Media, the market leader in online bidding services, to stop restricting customers from using rival platforms (ie, a wide MFN).

In January 2017, Amazon responded to European Commission concerns about parity clauses contained in contracts between Amazon and e-book publishers that required those publishers to inform Amazon about more favourable or alternative terms offered to Amazon's competitors and offer Amazon similar terms and conditions. Amazon agreed to scrap these clauses for a period of five years from August 2017.

In September 2017, the CMA opened an investigation into MFN clauses in ComparetheMarket's contracts with home insurers. In November 2018, it provisionally found that these clauses are in breach of UK and EU competition law as they prevented home insurance providers from offering lower prices elsewhere.

Another common form of pricing clause found in commercial agreements is the 'price matching' or 'English' clause. In such a clause, the supplier promises to (or is given the right to) match the lowest price offered to the distributor by any other supplier. This may be of benefit to the distributor by guaranteeing that it receives the best price available, but can potentially result in de facto exclusivity in favour of the supplier (see *Rangers Football Club and Sports Direct (SDI Retail Services Ltd v Rangers Football Club Ltd* [2018] EWHC 2772 (24 October 2018)).

In contrast to the complex retail MFNs that are widely under investigation, MFNs in distribution agreements may not always be problematic. They are particularly likely to raise competition concerns where the customer benefiting from the clause is dominant and the effect of the clause is to reduce the incentive of the supplier to offer other customers discounts, thereby aligning prices at a higher level than would otherwise be the case. This may not be very likely in most distribution scenarios and, in the absence of other restrictive effects, narrow MFNs may be enforceable. Each case should be assessed on the facts.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

On 3 December 2018, new rules came into force in the European Union and in the UK to prohibit the practice known as 'geo-blocking'. Geo-blocking affects sales made online: as soon as the credit card details reveal the location of the customer, the customer is directed to a local website that may charge higher prices. The new rules, set out in Regulation (EU) 2018/302 and the UK Geo-Blocking (Enforcement) Regulations 2018, identify three situations where geo-blocking is not justified:

- the sale of goods without physical delivery – if a Belgian customer wishes to buy a refrigerator and finds the best deal on a German website, the customer will be entitled to order the product and collect it at the trader's premises or organise delivery himself to his home;
- the sale of electronically supplied services – if a Bulgarian consumer wishes to buy hosting services for their website from a Spanish company, they will now have access to the service, can register and buy this service without having to pay additional fees compared to a Spanish consumer; and
- the sale of services provided in a specific physical location – an Italian family can buy a trip directly to an amusement park in France without being redirected to an Italian website.

However, suppliers are free to choose not to supply cross-border customers and need not harmonise their prices with those in other jurisdictions.

At the wholesale level, EU and UK competition law would step in where a supplier's discrimination in price is designed to penalise the

independent resellers: for low resale prices; for selling into a territory of another dealer (except where a geographical restraint is permissible); or for selling over the internet. Pricing to discourage any of these activities would also be caught. Price discrimination devised to restrict where buyers can resell the products will also infringe article 101 TFEU. This typically involves 'dual pricing policies', which offer discounts for products that are resold only locally or charge a premium price for products intended for export. Dual pricing will rarely be regarded as unilateral conduct. Rather, such policies are the result of vertical agreements between the supplier and distributor that have as their object or effect the restriction of intra-brand competition contrary to article 101(1) TFEU. In the *GlaxoSmithKline (GSK)* case, the ECJ concluded that, for an agreement to exist, it is sufficient for the parties to show a joint intention to conduct themselves on the market in a specific way. Signing the sales conditions (which contained dual pricing) and returning them to GSK indicated GSK's and the wholesalers' joint intention to adhere to the conduct and limit parallel trade. In the *GSK* case, the ECJ agreed that the dual pricing practised by GSK in Spain to deter (or make more expensive) purchases destined for export was an infringement of article 101 but did require that the Commission should not have refused to consider efficiency arguments before assessing them.

European Commission guidance provides that a dual-pricing agreement between a supplier and an independent distributor may fulfil the conditions of article 101(3) TFEU in some limited circumstances. For example, where offline sales include installation by the distributor but online sales do not, the latter may lead to more customer complaints and warranty claims and may therefore justify different pricing on- and offline.

Discriminatory pricing that places a trading partner at a competitive disadvantage by dominant companies (including discrimination based on nationality or location) for customers who are equivalent is prohibited unless the difference in treatment can be objectively justified (eg, by genuine cost savings or market conditions). The competitive disadvantage must be shown to distort competition for the discriminatory pricing practice to be unlawful (see the judgment of the ECJ in Case C-525/16, *MEO - Serviços de Comunicações e Multimédia SA* dated 19 April 2018). A dominant company is permitted to set different prices between various member states where there are already distinct geographical markets and the differences relate to the variations in the conditions of marketing and competition.

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

Generally, buyers (and their customers) should, in principle, be free to resell within the EEA without restraint. Restricting sales by the buyer outside specified territories or specified customers is a serious restriction permissible only under certain conditions, whether imposed directly (by contract) or indirectly (eg, by an incentive scheme). Schemes designed to monitor the destination of goods (eg, differentiating serial numbers) may be regarded as illegally facilitating market partitioning. The European Commission is currently investigating video game publishers and tour operators for restrictions in agreements with online distributors that they suspect discriminate between customers based on where they live ('geoblocking') and lead to partitioning of markets (see question 17).

However, there are some limited exceptions that allow market partitioning to some degree.

Exclusive distribution rights

A supplier may legally prevent a buyer from selling actively to customer groups or territories reserved exclusively for the supplier or to another buyer. 'Active sales' means actively approaching individual customers by, for instance, sending unsolicited emails or advertisements on the internet that are specifically targeted at customers in that territory. The supplier must not restrict a buyer's ability to make passive sales into reserved areas (ie, sales in response to unsolicited demand).

Consequently, other than the limited circumstances below, suppliers cannot offer distributors within the EEA absolute territorial

protection from parallel imports from other EEA territories even where they have an exclusive distribution network.

Territories or customer groups that are not allocated exclusively (ie, non-exclusive appointments or customers or territories reserved to supplier non-exclusively) cannot be protected either from active or passive sales.

However, restrictions on all sales, even passive sales, are acceptable in some exceptional cases, such as where they are necessary to create a new product market or to introduce an existing product on a new market. Even restraints on parallel imports will be acceptable for two years, insofar as intended to protect a distributor in a new geographical market.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

Suppliers should not impose an outright ban on internet selling by their distributors. This is regarded as a serious infringement of EU and, accordingly, UK competition law. In August 2017, the CMA fined Ping Europe Limited (Ping) for banning two of its retailers from selling online. Sales via the internet are generally viewed as passive (which cannot be restricted), except where adverts or marketing efforts are specifically aimed at customers in other territories. The ECJ has confirmed that internet sales must also be permitted by authorised distributors appointed in a selective distribution network (Case C-439/09 *Pierre Fabre Dermo-Cosmétique SAS v Président de l'Autorité de la concurrence and Ministre de l'Économie, de l'Industrie et de l'Emploi*). This means that online sales cannot be subject to geographical restrictions. The payment of 'invasion fees' would likely be considered as an indirect means of restricting internet sales, unless fees are in some way justified, for example, to cover the cost of repairs or servicing.

The ECJ has made an important distinction between an outright ban on internet sales by authorised distributors and the prevention of the discernible use of third-party platforms or marketplaces such as eBay and Amazon. In a case involving a reference from the German courts for a preliminary ruling, *Coty Germany GmbH v Parfumerie Akzente GmbH*, Case-230/16, the ECJ held that restrictions on third-party platforms are justified by the legitimate objective of preserving the quality and luxury image of the goods in question. This is subject to the proviso that the third-party platforms are subject to objective, qualitative criteria, which do not go beyond what is necessary to preserve the quality of the goods, and such criteria must be applied uniformly, and not in a discriminatory manner, to all potential platforms. It may be permissible to prevent online sales to protect brand image more generally in respect of non-luxury products, but this has not yet been tested. This type of restriction does not prevent distributors selling the goods online via their own websites or via third-party platforms that are not 'discernible' to the consumer.

There is a suggestion that any distribution system that qualifies under the VRBE could also have a platform ban, as such a ban is not a restriction of passive sales or a customer restriction.

There have been no EU cases on restriction on the use of price comparison websites by distributors, but it is possible that these may not be looked upon as favourably. In the *Coty* case, the court found the fact that authorised distributors could still advertise on price comparison websites to be a persuasive factor, suggesting that such a restriction may not be treated in the same way as a platform ban. Such websites are important in driving traffic to distributors' own websites. The German Supreme Court has ruled that Asics cannot impose a general ban on dealers using price comparison websites in the absence of any qualitative conditions. The Court did not consider running shoes to be luxury goods.

In December 2018, the EC fined Guess for imposing various restrictions on retailers in its selective distribution network:

- a ban on retailers using Guess brand names and trademarks in online search advertising;
- a requirement for retailers to obtain specific authorisation from Guess to make online sales (even though the retailers had already met the requirements for admission to Guess's selective distribution network);
- a ban on retailers selling to consumers located outside the retailers' allocated territories;
- restrictions on cross-selling between authorised wholesalers and retailers; and

- restrictions on the prices at which retailers could sell Guess products.

The EC found that these restrictions prevented retailers from advertising and selling Guess products cross-border, leading to artificially high retail prices in some member states. In addition to breaching competition law, some of these restrictions also breached Regulation (EU) 2018/302 and the UK Geo-Blocking (Enforcement) Regulations 2018 (see question 17 and 20). The EC's full infringement decision is expected to be made available in early 2019.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

Provided a supplier is not dominant, it can unilaterally refuse to deal with particular customers without breaching competition law.

A supplier can restrict a distributor's appointment to supplying a particular customer group, thereby preventing active sales by that distributor to other customers, provided those other customers are exclusively allocated to another distributor or reserved by the supplier. However, a distributor should not be prevented from making passive sales to customers outside its exclusive customer group or territory. The EC was investigating publishers of video games for 'geoblocking' (ie, preventing online customers in certain countries from benefiting from cheaper prices in neighbouring countries (see question 17)). In particular, it looked at whether agreements with online distributors prevent consumers from buying (or distributors from selling) activation codes in eastern Europe, where they are cheaper, for use in Western markets.

However, under the new Regulation (EU) 2018/302 and the UK Geo-Blocking (Enforcement) Regulations 2018, the provision of (non-audiovisual) copyright protected content services (such as e-books, online music, software and videogames) is not subject to the Regulation's prohibition of applying different general conditions of access for reasons related to a customer's nationality, residence or establishment, including by refusing to provide such services to customers from other member states. These services do still remain subject to the Regulation's prohibition to block or limit access to online interfaces on the basis of the nationality, residence or establishment of the customer. Where cross-border provision of these services takes place, the trader is prevented from discriminating the electronic payment means on the basis of the customer's 'nationality'.

A supplier can also prevent a distributor from selling to consumers, thereby keeping the wholesale and retail level of trade separate. However, it cannot otherwise agree with a distributor that it should not deal with particular customers. There are 'soft measures' that can be taken by suppliers to highlight to distributors the benefits of focusing on their allocated customers or territory. Such measures should not amount to an agreement, however, and distributors should not be penalised for doing so. Seemingly unilateral acts can be viewed as consensual. Where the supplier has established a selective distribution system or network it can prevent its distributors or dealers selling to resellers that are not approved members of that network.

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

It is highly unlikely that entering into a distribution agreement in itself would amount to a merger that could be subject to the merger control provisions of the Enterprise Act 2002 as amended by the Enterprise and Regulatory Reform Act 2013. There would have to be circumstances where a business obtains in relation to another:

- a controlling interest (de jure or legal control);
- de facto control (control of commercial policy); and
- material influence (ability materially to influence commercial policy).

The lowest threshold of material influence can be established through a range of factors, most obviously voting rights where shares above 15 per cent can be held to give material influence (and, in some cases, the authorities have required divestment to well below 10 per cent in

order to remove influence judged to be otherwise undesirable under relevant criteria). This assessment of influence may also occur where the minority shareholder is accorded special voting rights or veto rights, board representation or there is financial interdependence.

Acquiring rights of distribution in itself is unlikely to constitute a merger but where an entity, rights, a brand name, assets and contracts are acquired that may constitute the transfer of a business. The distribution rights may, however, be a factor taken into account in the assessment of influence. A good example in the United Kingdom was Heineken's acquisition of control over two Diageo subsidiaries:

The CMA considers that Heineken has already, on 7 October 2015, acquired legal control over D&G which owned the Target Brands and material influence over the Target Brands in Great Britain. This acquisition of material influence is further supported by the Manufacturing, Bottling, Selling, Distribution, and Marketing Agreement that is currently in place between D&G (now controlled by Heineken) and Diageo GB. However, with the transfer of the licence and distribution rights of the Target Brands to Heineken, Heineken will acquire a higher level of control (legal control) over these brands.

The merger control authority in the UK is the CMA and it has set out a range of relevant factors:

The transfer of customer records is likely to be important in assessing whether an enterprise has been transferred.

- *The application of the TUPE regulations would be regarded as a strong factor in favour of a finding that the business transferred constitutes an enterprise.*

- *The CMA would normally (although not inevitably) expect a transfer of an enterprise to be accompanied by some consideration for the goodwill obtained by the purchaser. The presence of a price premium being paid over the value of the land and assets being transferred would be indicative of goodwill being transferred.*

4.9 Outsourcing arrangements involving ongoing supply arrangements will not generally result in enterprises ceasing to be distinct, but may do so where, for example, they involve the permanent (or long-term) transfer of assets, rights and/or employees to the outsourcing service supplier and where those may be used to supply services other than to the original owner/employer. The CMA will assess whether, overall, the assets, rights and employees transferred to the outsourcing service supplier are such as to constitute an enterprise under the principles set out above.

Mergers: Guidance on the CMA's jurisdiction and procedure (CMA2)

The assessment of the merger, assuming it constitutes a 'merger' under the UK regime, will ultimately be whether the transaction is found to result, or is expected to result, in a substantial lessening of competition in the UK. In the distribution context, the issue will often be whether there is foreclosure of a supplier or of a distributor. Not every transaction that is a merger is examined; there is no obligation to pre-notify, although, where the authorities have jurisdiction, it may be sensible to do so. The authorities have no jurisdiction to look at a merger unless as a result of the transaction the merged entity's share of supply or purchases, of goods or services of a particular description in the UK or a substantial part of the UK, exceed 25 per cent, or such a share of supply (not to be confused with market share) is increased. If the target acquired has a turnover of at least £70 million in the UK, the authorities also have jurisdiction irrespective of the share of supply.

As a result of the Enterprise Act 2002 (Turnover Test) (Amendment) Order 2018 (Turnover Test Order 2018), which came into effect from 11 June 2018, investments in the defence, dual use, quantum tech and CPU sectors are subject to a reduced threshold of £1 million for triggering a relevant merger situation (which may result in an investigation by the UK CMA). Additionally, the Enterprise Act 2002 (Share of Supply Test) (Amendment) Order 2018 (Supply Test Order 2018), which also came into effect from 11 June 2018, provides that the acquisition of a company in one of the above sectors (with a 25 per cent share of supply of goods or services in the UK pre-merger) will also trigger a relevant merger situation.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

Market studies

The UK competition authority, the CMA, has powers to intervene and conduct studies of particular markets and this could impact on distributor supplier relationships. An example is the investigation of the market for aggregates, cement and ready mixed concrete, which resulted in divestment orders and a ban on suppliers issuing generic price announcement letters. The CMA has also investigated the role of digital comparison tools across a range of product and service markets and has identified concerns about lack of transparency over whether suppliers can influence how products are presented on such tools as well as potential competition concerns about whether certain clauses in contracts between suppliers and providers of tools could limit price competition or innovation, or restrict market entry. A report published in 2017 set out a number of recommendations for online comparison tools, including clearly displaying product and price information, and informing users on how their personal data will be used. This also triggered an investigation into a particular price comparison website's contracts with home insurers to determine whether they were pushing up the prices for consumers (see question 16).

Court actions under competition law

Parties can bring actions of various kinds for breaches of competition law. Those that have suffered loss as a result of a breach of competition law will have a claim in damages. Such claims can be stand-alone claims (where the claimant needs to prove the breach of competition law, causation and loss) or 'follow-on' actions (where the claimant can rely upon a decision of a competition authority finding that a party has breached competition law as proof of that breach). In a follow-on action, the claimant must, therefore, prove only causation and loss.

In the distribution context, a distributor may be able to claim damages if, for example, the supplier has been engaged in price-fixing with other suppliers and the prices paid by the distributor are higher than they might otherwise have been, but the distributor would have to show it did not pass on any overcharge. Suppliers or distributors may face claims for damages for abuse of a dominant position. Labinvesta raised proceedings in November and December 2016 against a supplier of consumables used in medical treatment and its subsidiary distributors, alleging that the defendants had unlawfully refused to supply products to Labinvesta for onward distribution in Belarus (CAT Case No. 1273/5/7/16). This case has now been withdrawn.

Similarly, a party may be able to claim damages even if it is a party to an agreement that is anticompetitive provided the party seeking to claim damages was in a weaker position than the other party in the negotiation of the contract such that it was not genuinely free to choose the terms of the contract (*Courage v Crehan* [2002] QB 507).

Damages in the UK are generally compensatory. Punitive damages are not available in the UK for breach of contract.

More commonly in distribution disputes, parties can use competition law to defend court action if, for example, the clauses being sued upon are unenforceable because they restrict competition.

However, in the case of *James McCabe v Scottish Courage* [2006] EWHC 538 (Comm), regarding the severability of an exclusivity provision that was potentially anticompetitive, the court held an exclusivity provision (which was unlawful) could not be severed from the agreement as to do so would damage the fundamental nature of the agreement between the parties and that the clause was instrumental in inducing the supplier to enter into the contract in the first place. If the clause is unlawful and is key to the agreement, the whole agreement is unenforceable.

Parties can bring an action in the Competition Appeal Tribunal (CAT) or the High Court for damages or for injunctions. The CAT obtained additional powers in respect of stand-alone damages claims for competition law breach and for injunctions as a result of the Consumer Rights Act 2015 from 1 October 2015. Its jurisdiction to issue injunctions does not extend to Scotland. It also introduced an opt-out collective claim procedure to operate alongside an opt-in procedure. The first opt-out collective claim was raised as a 'follow-on'

action for damages arising from the OFT *Mobility Scooters* decision that found a manufacturer of mobility scooters guilty of prohibiting online advertising of prices below the manufacturer's recommended retail prices (*Dorothy Gibson v Pride Mobility Products Ltd*, CAT Case No. 1257/7/7/16). This was subsequently abandoned after the CAT ordered that the scope of the claimants' arguments be narrowed to reflect only the loss that they themselves suffered and that more economic data should be provided to support their claim. A second-class action was dismissed by the CAT in July 2017. A former financial services ombudsman sought damages on behalf of millions of consumers on the basis of a 2007 European Commission decision that said that MasterCard had been charging customers anticompetitive card fees for 18 years (*Walter Hugh Merricks v Mastercard and others*, CAT Case No. 1266/7/7/16) but was unsuccessful in convincing the Tribunal that he could quantify the loss suffered by each member of the class or prove the harm he alleged occurred. Permission from both the Administrative Court of the High Court and the Court of Appeal to challenge the ruling has been granted.

The Consumer Rights Act (CRA) 2015 introduced a 'fast-track' procedure, intended to make it quicker and cheaper to obtain a remedy for harm suffered as the result of anticompetitive behaviour, with limited exposure to costs risk. Though intended to make it easier for individuals and small and medium-sized entities, it is not restricted to them. To be suitable for the 'fast-track', a case must be brought to trial within no more than six months of allocation and, in general, the trial must take no longer than three days. Therefore, it was thought that use of the 'fast track' might be restricted to straightforward cases involving few parties and not requiring significant disclosure or extensive expert evidence. The procedure has proved popular, particularly in cases involving an alleged abuse of a dominant position. One such case proceeded to trial (*Socrates Training Limited v The Law Society of England and Wales*, CAT [2017] CAT 10), with others settling. Although the 'fast track' might have been thought suitable only for cases in which the relief sought is limited to a finding of infringement and the grant of an injunction (eg, to restrain further infringement, to require a resumption of supplies or to grant access to an 'essential facility'), most cases have also involved a claim for damages. In 2016, a claim for damages that followed from the European Commission's *Polyurethane Foam* decision was refused allocation to the fast track as it raised complex issues that could not be dealt with in three days (*Breasley Pillows Limited and Others v Vita Cellular Foams (UK) Limited and Others* [2016] CAT 8).

23 Are there ways in which a distributor or agent can prevent parallel or 'grey market' imports into its territory of the supplier's products?

Some limited protection from active sales efforts that constitute parallel imports is obtained by appointing distributors exclusively for particular territories and seeking to prevent active sales between those territories. It may also be helpful to keep the wholesale and retail level of the market separate. However, the concept of passive sales in the EEA means that no system is watertight against passive sales; it is difficult to take action against parallel imports without there being some element of risk or uncertainty.

Another option, where appropriate and justified by the nature of the products, is to set up an EEA-wide selective distribution system. Although sales between authorised distributors across borders cannot be prevented in such systems, sales to unauthorised distributors can be. However, all authorised distributors must be able to make active and passive sales to consumers (including over the internet), subject to the supplier being able to require that sales are made from a particular location, so again, parallel sales cannot be ruled out. As discussed in question 19, online sales via third-party platforms can lawfully be prevented to protect the luxury image of the goods that are subject to a selective distribution system (*Coty Germany GmbH v Parfümerie Akzente GmbH* (Case C-230/16)). It may be permissible to prevent online sales to protect brand image more generally, but this has not yet been tested. Outright bans on selling online are not permissible.

Certain steps can, however, be taken to educate the distributor on the problems of parallel imports; that does not amount to an agreement not to make passive sales across borders. However, care should be taken with this approach as it can easily stray into an agreement to prevent passive sales:

- clear communication about the brand standards that are expected is important, including clear, objective and consistent quality standards for websites and shops;
- it could be made clear to the distributor that the supplier will not increase its marketing support should sales be boosted by orders from outside of their channel or territory;
- it could be agreed with the distributor that the resource involved in selling into the approved channel is maintained at all times (ie, is not reduced as a result of making passive sales outside the territory);
- the supplier could require that the distributor explains in marketing materials the benefits of buying locally from that distributor; and
- the supplier is permitted to discuss the effect that parallel trade has on margins with a distributor, provided it does not penalise the distributor for selling outside its territory or channel.

UK (and EU) trademark legislation allows trademark proprietors to object to the importation of products from outside the EEA into the UK or EEA if they have not consented to these goods being sold in the EEA.

Proprietors can also object to the importation of genuine products originally authorised by them for sale elsewhere in the EEA, if there are legitimate reasons for the proprietor to oppose further dealings in the goods. Legitimate reasons include: where the condition of the goods has changed; where the goods have been repackaged in breach of conditions set out in case law; and where luxury goods have been resold outside the proprietor's selective distribution network.

The case law suggests that proprietors can object to sales by the distributor to resellers outside the selective distribution network if they can show that further sale by the resellers, for example, to non-authorised discount stores, will seriously damage the reputation of the trademark (*Copad v Christian Dior*, Case-59/08).

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

UK legislation and industry codes of practice regulate the advertising and marketing of products. These are standard rules, not specific to distribution arrangements. The rules apply when marketing to businesses and consumers. The rules aim to ensure that all advertising is legal, decent and not misleading. Industry-specific rules also apply in areas such as pharmaceuticals and food and drink.

Other than as set out above, parties to a distribution contract are generally free to agree terms relating to advertising. Further, suppliers can retain complete control over all marketing. However, more typical advertising provisions in distribution agreements include:

- making the distributor responsible for advertising in its territory, and the associated costs;
- setting a minimum annual expenditure on advertising (often a percentage of turnover);
- using only materials provided by or approved by the supplier; and limiting a distributor's freedom to actively advertise in territories other than its own (see question 18).

As advertising will require use of the intellectual property rights of the supplier, distribution agreements typically include an express licence of those rights, and express terms requiring the supplier's prior consent before advertising material is made public. It is also typical to require distributors to adhere to instructions issued by a supplier regarding all advertising materials and to assign all goodwill in the use of the supplier's branding to the supplier.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

Suppliers would typically seek to safeguard their intellectual property rights (IPR) from infringement by distribution partners through the express terms and protections which would be set out in the distribution agreement. Some of the typical provisions used to protect IPR from such infringement include:

- obligations on the distributor to refrain from doing anything that may infringe or devalue the IPR in question;

- prohibitions on distributors applying for a registered trademark that is identical, or similar to, the supplier's;
- prohibitions on distributors registering domain names that incorporate the supplier's trademarks or using a company or trade name that is identical or similar to the supplier's;
- prohibitions on distributors selling competing products although the term of such clauses must be less than five years to benefit from EU competition law exemptions (see question 13);
- requirements for distributors to seek the prior consent of the supplier before producing advertising material incorporating the supplier's IPR;
- obligations on distributors regarding the transfer and use of confidential information and trade secrets; and
- assignments of goodwill generated by the distributor using the supplier's branding to the supplier.

It is also common for suppliers to include terms in a distribution agreement to help protect against third-party infringement. Some typical provisions include requiring a distributor to notify the supplier of any third-party IPR that is, or that may be, infringing the supplier's IPR and cooperate in any IPR infringement proceedings against third parties.

Although it is common for distribution agreements to contain licence terms for branding, it is less common for patents. If patents are relevant, the parties would typically enter a separate patent licence agreement. The Technology Transfer Block Exemption Regulation 2014 (TTBER) exempts such agreements from assessment under competition law subject to fulfilling certain criteria, including market-share thresholds. Such agreements would typically include provisions allowing the supplier to terminate the contract if the distributor challenges its IPR. However, including this term in a non-exclusive licence would remove the benefit of TTBER and expose the agreement to assessment under competition law.

26 What consumer protection laws are relevant to a supplier or distributor?

There is a wide range of consumer protection laws that are relevant to business to consumer sales. These are summarised very briefly below:

- The Consumer Rights Act – the CRA 2015 applies to contracts entered into on or after 1 October 2015. The CRA consolidated the previously fragmented approach to UK consumer law and reformed many aspects of consumer law in the UK. The CRA sets out statutory rights and tiered remedies for consumer contracts for goods and services, and introduces a new category of contract for the supply of digital content. The law on unfair contract terms in consumer contracts has been reformed by the CRA and private actions for breach of competition law have been introduced. The powers of enforcement authorities under some consumer protection legislation are also reformed.
- The Consumer Contracts (Information, Cancellation and Additional Charges) Regulations 2013 – these implement most of the Consumer Rights Directive (2011/83/EU). They provide a range of consumer rights in relation to contracts for goods or services (but do not apply either in part or in their entirety to certain types of contract). These rights include the provision of certain information to consumers, a right for consumers to cancel certain contracts within 14 days after the contract was entered into; and rights for consumers to receive a refund and information on certain other prescribed aspects of a contract.
- The Consumer Protection from Unfair Trading Regulations 2008 – these prohibit consumer sales practices that are misleading by action or omission or are otherwise unfair or are aggressive. In 2014 they were amended to introduce a new direct civil right of redress by consumers against traders who conduct misleading or aggressive practices.
- The Electronic Commerce (EC Directive) Regulations 2002 – these place requirements on information service providers about how contracts concluded through electronic means will be made.
- Provision of Services Regulations 2009 – these require that the service provider must (i) provide consumers with certain information about itself; (ii) deal with customer complaints promptly; and (iii) not discriminate against consumers in the provision of services on the basis of place of residence (unless such different treatment can be objectively justified).

Contracts entered into with consumers before 1 October 2015 may require consideration of legislation that is no longer in force or that no longer governs business-to-consumer arrangements, including:

- the Sale of Goods Act 1979 (SGA);
- the Supply of Goods and Services Act 1982 (SGSA);
- the Unfair Terms in Consumer Contracts Regulations 1999;
- the Unfair Contract Terms Act 1977; and
- the Consumer Protection (Distance Selling) Regulations 2000.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

The General Product Safety Directive 2001/95/EC (implemented in the UK by the General Product Safety Regulations 2005) requires products placed on the market to be safe. Where a product presents risks to safety, recall will be a last resort where other measures would not prevent the risks involved. Product recall can be undertaken voluntarily or at the request of a relevant authority (which in the UK are the trading standards department of local authorities). Distributors are expected to cooperate with the manufacturer to avoid risks or implement a recall if this is deemed necessary. A distributor is capable of having the same obligations as the producer of the product it is handling. For example, a distributor (and producer) is obliged, where it discovers a product it has placed on the market is unsafe, to notify the local authorities and provide information on the action they plan to take. A distributor is under an obligation to act with due care to ensure products supplied are safe.

The parties are free to agree which party is responsible for carrying out and absorbing the cost of a product recall. However, a manufacturer cannot contract out of liability to a consumer that has suffered harm as a result of an unsafe product.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

A business cannot exclude or limit liability for its own fraud. The extent to which warranties and liabilities can be excluded or limited differs in some aspects between B2B contracts and consumer contracts.

Business-to-business

- The UCTA provides that a business cannot exclude liability for death or personal injury as a result of negligence;
- the Consumer Protection Act 1987 prevents a business from limiting or excluding liability for death, personal injury or loss of or damage to property caused by defective products; and
- the SGA implies a number of warranties in contracts for the sale of goods (and this area has been consolidated to a large extent by the CRA in respect of terms implied into consumer contracts); including good title to sell the goods and that the goods are as described, of satisfactory quality and fit for purpose, and conform to any sample provided in terms of quality. Suppliers can expressly exclude the implied terms in relation to the quality of the goods, subject to the reasonableness requirement under the UCTA. However, the implied term as to good title and no encumbrances cannot be excluded.

Otherwise, a party is free to limit liability for loss or damage caused by negligence, subject to a test of reasonableness under the UCTA. What is reasonable is a question for the courts. The onus to prove a clause is reasonable is on the party wishing to rely on it. The courts, when applying the reasonableness test, take account of the circumstances in which the parties entered into the Agreement, including:

- the relative bargaining positions of the parties;
- whether the customer received an inducement to agree to the term; and
- whether the customer knew or ought reasonably to have known of the existence and extent of the term.

Liability for certain acts or omissions not involving negligence but that relate to breach or non-performance of contract or performance different from that reasonably expected, will be subject to the UCTA only when found in written standard terms of business. Such exclusions or limitations of liability will be subject to the reasonableness test. There

is no statutory definition of 'written standard terms of business'. UCTA does not apply to contracts that have been individually negotiated, or that a party sometimes uses and sometimes does not, but only to terms which are not negotiated and are habitually used by the party relying on them.

Further, the recent case of *Goodlife Foods Ltd v Hall Fire Protection Ltd* [2018] suggests that where the party seeking to rely on a limitation of liability clause offers the other party an alternative (eg, an option of insurance to enable them to accept a wider scope of liability), the limitation clause is more likely to be reasonable.

Terms that exclude or restrict liability for misrepresentation are subject to the Misrepresentation Act 1967 and the UCTA reasonableness test. Language that provides that no warranties have been made or relied on (frequently included as part of entire agreement clauses) is also likely to be subject to the UCTA. In *IFE Fund SA v Goldman Sachs International* [2006] EWHC 2887 (Comm), the court noted that whether a clause amounts to an exclusion clause is a 'question of substance, not form'. *Cremdean Properties Ltd v Nash* [1977] EGLR 80 provides authority for the principle that a party cannot, by a carefully chosen form of wording, circumvent the legislative controls on exclusion of liability for misrepresentation.

The Court of Appeal has now confirmed in the recent case of *First Tower Trustees Ltd v CDS (Superstores International) Ltd* [2018] EWCA 1396 that a non-reliance statement is always potentially an exclusion of liability for misrepresentation. They expanded to say that when faced with a non-reliance statement, there are two relevant questions of fact:

- Does the non-reliance statement have the effect of excluding or limiting the alleged representor's liability for misrepresentation, or the remedies available to the alleged representee for misrepresentation?
- If so, does the exclusion or limitation pass the UCTA reasonableness test?

Consumer contracts

The CRA provides that a business cannot exclude liability for death or personal injury as a result of negligence. None of the terms implied by the CRA, including those relating to the quality of the goods digital content or services or both, can be excluded. Exclusions and limitations of liability (including for breaches not involving negligence) in consumer contracts are subject to the reasonableness test under the CRA. This test may be difficult to satisfy in consumer contracts, particularly if there is a blanket exclusion.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

The legal regulation of distributors sharing customer data with suppliers and to organisations dealing with personal data, which in this context is likely to include customer data is set out in the Data Protection Act 2018 and the General Data Protection Regulation (Regulation (EU) 2016/679) (GDPR). The legislation is not specific to distribution arrangements and applies to the UK and all the member states from 25 May 2018. The GDPR is likely to cease to be of effect if the UK exits the EU on 29 March 2019 but the Data Protection Act 2018 will remain part of UK law and it is expected that the GDPR will be incorporated into the UK law to sit alongside the Data Protection Act 2018.

Under the current legislation, individuals must be informed about the data that is being collected about them, how this data will be used and the details of the parties collecting and using the data. The party that determines how the data shall be processed is deemed to be the data controller of that data (ie, a person who decides 'why' and 'how' that data will be processed). It is the data controller who is responsible for complying with the applicable law. UK privacy regulations also impose limits on the use of individuals' data for marketing. Failure to comply with the data protection and privacy rules has the potential to lead to significant fines. However, these are typically reserved for only the most serious breaches.

If a supplier imposes an obligation on a distributor to share end customer data within the distribution agreement, supplementary obligations should be included requiring the distributor to present appropriate privacy notices to end customers and, where necessary, to obtain

the necessary consents from the end customers to facilitate both the sharing with the supplier, and the supplier's subsequent use of the data.

Transfers of personal data outside the EEA must comply with a range of requirements. Transfers outside the EEA are permitted where the individual has consented to the transfer or the transfer is necessary for the performance of the contract with the individual. Transfers outside the EEA are also permitted if the country to which the personal data is transferred has been approved as offering an adequate level of protection. The European Commission maintains a list of approved countries (which does not include the United States).

If no finding of adequacy has been made in respect of a country outside the EEA, a business can transfer data internationally within its corporate group subject to Binding Corporate Rules provided they are specifically recognised by an EU data protection authority, including the UK Information Commissioner's office, or by including the European Commission-approved model contract clauses.

The European Commission also adopted the EU-US Privacy Shield on 12 July 2016 to facilitate transfers to the United States. The arrangement provides stronger obligations on companies in the United States to protect the personal data of Europeans and stronger monitoring and enforcement by the US Department of Commerce and Federal Trade Commission, including through increased cooperation with European Data Protection Authorities. The arrangement includes commitments by the United States that possibilities under US law for public authorities to access personal data transferred under the Privacy Shield will be subject to clear conditions, limitations and oversight, preventing generalised access. Businesses transferring personal data are advised to rely on European Commission-approved model contract clauses or Binding Corporate Rules.

Finally, transfer of personal data outside the European Union is also permitted where the individual has explicitly consented to the transfer or the transfer is necessary for the performance of the contract with the individual.

The adoption of the Data Protection Act 2018 and the GDPR brought about:

- a single legal framework that applies in each individual EU member state as well as the UK. This has resulted in a more consistent approach to data protection compliance across Europe;
- more onerous obligations regarding obtaining consent from individuals. Consent to processing must involve a clear affirmative action and must be 'freely given, specific, informed and unambiguous' under the GDPR and, where special category is involved, consent must also be explicit;
- direct statutory obligations on processors, as well as controllers;
- greater regulation of the transfer and processing of personal data outside the European Union (in certain circumstances);
- significant increases in potential fines for controllers. Certain breaches could incur a fine of €20 million or up to 4 per cent of the controller's total global annual turnover; and
- more onerous obligations in respect of accountability for both controllers and processors, including a requirement to maintain records of personal data being processed (and to make these available to the supervisory authority on request).

If not already done, urgent steps should be taken now to ensure that the exchange of customer data will comply with the GDPR. Distribution agreements now typically contain fuller data-protection clauses or include a data-protection schedule that will set out more stringent measures that parties will need to adhere to in relation to processing customer data.

The European Commission also adopted the EU-US Privacy Shield on 12 July 2016 to facilitate transfers to the United States. The arrangement provides stronger obligations on companies in the United States to protect the personal data of Europeans and stronger monitoring and enforcement by the US Department of Commerce and Federal Trade Commission, including through increased cooperation with European Data Protection Authorities. The arrangement includes commitments by the United States that possibilities under US law for public authorities to access personal data transferred under the Privacy Shield will be subject to clear conditions, limitations and oversight, preventing generalised access. Businesses transferring personal data are advised to rely on European Commission-approved model contract clauses or Binding Corporate Rules.

Any sharing of data between a data controller and another party should be in writing and comply with Data Protection Legislation. Data sharing should take place subject to contractual obligations to ensure personal data are kept secure and processed only in line with data protection principles.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

The courts will be reluctant to intervene when the parties have agreed clear and unambiguous provisions to govern their contractual relationship. Therefore, in principle, the supplier is entitled to insist on a contractual right to object to the management of the distributor. A termination right for the supplier in the event of dissatisfaction with the distributor's management is, however, a wide and subjective provision, so could be the subject of dispute before the courts. Targeting individuals whose employment may be jeopardised is not without risk. Care should be taken as regards the criteria for objecting, especially where it does not have a link with economic performance: a claim of discrimination on, among others, race, creed, sexual orientation, gender, disability or age would be a serious issue.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

There is a risk that a distributor or agent could be treated as an employee of the supplier. This will be determined by the nature of the relationship in practice. The degree of mutuality of obligation, the control exercised by the supplier over the distributor or agent and whether work has to be performed personally by the distributor or agent are the principal determining factors. Additionally, where a distributor or agent is a company, their employees and employment liabilities could be transferred to the supplier where, after the termination of the distribution or agency agreement, the supplier proposes to bring the distribution or agency services in-house (see Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE)).

If it is determined that a distributor or agent is an employee of the supplier, the supplier is liable as the employer for the entire employment. If an employee of a distributor or agent becomes an employee of the supplier through TUPE, their normal terms and conditions of employment will apply post-transfer, their continuous service will be unbroken and the supplier will inherit all employment liabilities. For example, if the distributor or agent provided sick pay benefit over and above the statutory regime, the supplier would be contractually obliged to provide the same benefit post-transfer, even if none of its own employees is so entitled. All the usual UK employment rights would also apply to these employees, including holiday pay, national minimum wage, statutory sick pay, maternity, paternity, parental and adoption rights (including statutory payments), statutory notice, auto-enrolment in a pension scheme and, after two years' continuous service, a right not to be unfairly dismissed and a right to a statutory payment if made redundant.

To protect itself, a supplier would generally ask the distributor or agent to indemnify them against any employment liability as part of the distribution or agency agreement. This would include a clause splitting employment liabilities between the parties according to whether they arose before or after the transfer date. Indemnities in respect of the application of TUPE are usually very detailed and are a point for negotiation between contracting parties.

32 Is the payment of commission to a commercial agent regulated?

Yes. The Agency Regulations prescribe for the circumstances in which an agent will be entitled to the payment of commission (Agency Regulations 7-9):

- 7.—(1) A commercial agent shall be entitled to commission on commercial transactions concluded during the period covered by the agency contract—*
- (a) where the transaction has been concluded as a result of his action; or*

- (b) where the transaction is concluded with a third party whom he has previously acquired as a customer for transactions of the same kind.
- (2) A commercial agent shall also be entitled to commission on transactions concluded during the period covered by the agency contract where he has an exclusive right to a specific geographical area or to a specific group of customers and where the transaction has been entered into with a customer belonging to that area or group.

Broadly, the agent is entitled to 'reasonable remuneration taking into account all aspects of the transaction'. This includes commission on transactions concluded during the term of the agency relationship arising in whole or in part as a result of the agent's actions; and transactions concluded after termination of the agency relationship that are 'mainly attributable' to the agent and are concluded within a 'reasonable period' after the agency contract terminated. 'Mainly attributable' requires a causal link between the agent's activities and the contract being concluded and is not thought to be different from effective cause (*PJ Pipe & Valve co Ltd v Audco India Ltd*, [2005] EWHC 1904 (QB)). What is a reasonable period after termination will vary according to the facts and context but, in one case, nine months after termination was a reasonable period.

In *Georgios Kontogeorgos v Kartopak AE* (Case C-104/95 [1997] 1 CMLR 1093), the Court of Justice held that a commercial agent who is in charge of a particular area has a right to commission even if the contracts are concluded without the agent's intervention (eg, the principal concludes the contracts directly). The same would apply in respect of orders from a group of customers for whom the agent was responsible. However, it is clear that the agent is not entitled to commission when it is a third party selling into the exclusive territory or customer group rather than the principal (Case C-19/07 *Heirs of Paul Chevassus-Marche v Groupe Danone*).

The timing of when commission becomes due and when payment of commission should be made is also covered by the Agency Regulations (Regulation 10).

Recently, the ECJ has confirmed that commercial agents will be entitled to indemnity or compensation even where termination occurs during a contractual trial period (*Conseils et mise en relations (CMR) SARL v Demueures terre et tradition SARL* (C-645/16) EU:C:2018:262).

33 What good faith and fair dealing requirements apply to distribution relationships?

Contract law does not recognise a general implied duty to perform contracts in good faith. This differs from the situation in many other countries, including France and Germany, which recognise some form of implied term that in agreeing and performing contracts the parties should act in good faith.

However, the courts are willing to give effect to express obligations to act in good faith in a wider range of commercial contracts and, in some instances, have shown that they are prepared to imply a duty of good faith. The meaning and effect of good faith are likely to vary considerably depending on the context. Broadly, a good faith requirement involves acting with honesty, genuineness and integrity.

The case of *Yam Seng PTE Ltd v International Trade Corporation Ltd* [2013] EWHC 111 (QB) is significant as the High Court implied a duty of good faith to a distribution agreement. The claimant, Yam Seng, entered into a distribution agreement with the defendant, ITC, pursuant to which ITC granted Yam Seng the exclusive rights to distribute certain fragrances bearing the brand name 'Manchester United' in specified territories in the Middle East, Asia, Africa and Australasia. The contract period initially ran from 12 May 2009 until 30 April 2010, but was later extended until 31 December 2011. The judge determined that ITC was in breach of certain express terms of the contract. The judge found that one breach was repudiatory, but also went on to consider whether a duty of good faith was to be implied into the contract.

The court suggested that in some B2B contracts, good faith should be implied into the contract between two businesses, especially where the type of contract, such as a distribution agreement, involves one or both parties having to expend considerable time, effort and money in preparing to put the contract into practice. The judge explained the importance of good faith and fair dealing in 'relational contracts' such

as joint venture agreements, franchise agreements and long-term agreements.

However, UK courts are still generally reluctant to imply terms into contracts. In *Ikerler Otomotiv Sanayai VE v Perkins Engines Company Ltd* [2017] EWCA Civ 183, a distributor argued that its supplier owed it an implied duty of good faith as regards the supplier's ability to terminate. The Court of Appeal rejected any such argument. The general principle for this decision is that termination is absolute contractual right, not a discretion that must be exercised fairly (*Monde Petroleum v Westernzagros Ltd* [2018] EWCA Civ 25). The test for implying a duty of good faith into a contract is the same as for implying any term, being that, only if, without such an implied term, the contract would lack commercial common sense should the duty be implied (*Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd* [2015] UKSC 72 and *Monde Petroleum v Westernzagros*). In *Astor Management AG v Atalaya Mining Plc* [2017] EWHC 425 (Comm), the court summarised that the position on the duty of good faith (where it exists) reflects the expectation that a contracting party:

- will act honestly towards the other party; and
- will not conduct itself in a way that is calculated to frustrate the purpose of the contract or which would be regarded as commercially unacceptable by reasonable and honest people.

There is also a general principle, now established in English law, that, in exercising a contractual discretion, a party must act in good faith and not arbitrarily or capriciously (*British Telecommunications plc v Telefonica O2 UK Ltd* [2014] UKSC 42). The purpose of the duty is to prevent abuse of a party's role as decision maker. Therefore, it won't apply to the exercise of an absolute contractual right (such as a termination right) nor a clause which calls for the objective assessment of a matter. In a distribution context, the supplier may be required to act in good faith (most likely meaning 'rationally' but subject to the exact wording of the contract) if it has a right that allows it to unilaterally adjust the commission due to its distributor.

The relationship of agent and principal includes a fiduciary duty at common law in favour of the principal specifically to avoid a conflict with the agent's main interests and not to profit from its position at the expense of its principal.

The Commercial Agents Regulations state that a commercial agent must look after the interests of his principal and act dutifully and in good faith (Regulation 3(1)). Likewise, a principal has an obligation of good faith towards his agent (Regulation 4(1)).

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

No. However, it is considered best practice to register any agreement that includes a licence of a patent, registered trademark or registered design with the UK Intellectual Property Office.

Although it is not common practice, the parties to a distribution agreement that includes a licence of registered trademarks, registered designs or patents, may consider detailing this licence in a separate document annexed to the main distribution agreement. The benefit of this approach is that the licence can then be registered separately from the main distribution agreement, therefore protecting the commercial terms from potential public disclosure.

The benefits of registering licences include:

- if the IPR are later sold to a third-party purchaser, they are sold subject to the burden of the registered licence. This means even where the third-party purchaser was unaware of the licence, they are required to honour it going forward;
- similarly, if the owner of the IPR attempts to grant an exclusive licence that would conflict with the pre-existing registered licence, the original licensee's position is protected and their licence stands;
- in respect of licences of registered trademarks (common in distribution arrangements to allow the distributor to carry out advertising), unless the licence states otherwise, registration grants the distributor the right to call upon the supplier to take action to prevent others from infringing the trademark, and the right to bring infringement proceedings if the supplier fails to do so. If the licence is exclusive, the licensee may be entitled to bring proceedings in its own name; and

- in respect of licences of patents (in the unusual scenario where a patent is licensed to a distributor), if the distributor is an exclusive licensee then it will be entitled to bring infringement proceedings in its own name.

It should be noted that the registration of the IP licence will be primarily for the benefit of the distributor or licensee, rather than the supplier or licensor.

Finally, failure to register a registered trademark licence or patent licence within six months may affect the amount of damages that can be recovered by the distributor in a court action for infringement.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

The UK's Bribery Act 2010 very much applies to the relationship between suppliers and distributors. A distributor may offer or give a bribe in order to win orders or retain business. If it does so with the connivance or knowledge of the manufacturer, supplier or brand owner then both will have committed an offence.

In addition, a distributor, as with local consultants, agents, licensees or joint venture partners can be regarded as associated persons in relation to a manufacturer or supplier; they perform services for or on behalf of the supplier. Under the Bribery Act 2010, even where a supplier has no knowledge or indication that an associated person has offered or given a bribe, the supplier may commit the offence under section 7 of the Act of failure to prevent bribery where the offer was intended to obtain or retain business for or on behalf of the supplier. If it can demonstrate that the offence took place despite all its measures taken to prevent bribery by associated persons and that those measures are viewed as adequate then it will have a defence. Such measures will include taking all reasonable diligence commensurate with the geographical or sector risk or other risk factors (such as links the agent or distributor may have with public officials or with private buyers).

Therefore, when appointing a distributor, a supplier should undertake some diligence on the risks of bribery. It should ascertain whether the distributor or agent has any history of involvement or accusations of involvement in such activities; likewise it should determine whether the distributor or agent has an anti-bribery policy of any worth. It should make clear, in writing preferably, that avoiding bribery including facilitation payments is an essential policy with which compliance is required. The scope of the UK Bribery Act (extending to bribery of private persons, not solely public officials and covering facilitation payments). The need to avoid lavish entertainment of relevant decision makers should be made clear. The supplier should also contractually require compliance with all bribery laws and seek to be indemnified for losses it might incur should there be bribery proceedings or investigations. It is also possible that a supplier might bribe a customer or an official where that brings or retains business for the distributor or agent. It is not likely that the supplier would be an associated person as it does not normally perform services on behalf of the distributor or agent. Therefore, assuming the distributor or agent is not conniving with the supplier in respect of the bribery, it is not likely to incur liability. Nevertheless, it would be advisable for a distributor or agent to require contractually that the supplier comply with anti-bribery laws and indemnify against the costs of any investigation and loss of business.

The UK Supreme Court confirmed that where an agent accepts a bribe or secret commission in breach of his or her fiduciary duty, it is considered the property of his or her principal who may then reclaim the wrongfully received benefit (*FHR European Ventures LLP & Ors v Cedar Capital Partners LLC* [2014] UKSC 45).

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

Contracts may include implied contractual terms that have not been expressly agreed between the parties but are deemed to be incorporated into the contract by a court as a result of: usage or custom; the previous course of dealings of the parties; the intentions of the parties; common law; and legislation. These rules are not specific to distribution contracts.

Examples of the legislation most relevant to distribution agreements and that imply contractual terms and that have been discussed in this chapter include the SGA, SGSA, Misrepresentation Act 1967, UCTA and Consumer Rights Act 2015.

Others include:

- the Late Payment of Commercial Debts (Interest) Act 1998 – assesses and implies terms relating to payment, including the level of interest that shall be payable on outstanding amounts due under a contract unless the contract specifies otherwise; and
- the Contracts (Rights of Third Parties) Act 1999 – allows a third party to enforce a contract term where the contract specifically provides for this; or a term confers a benefit on a third party and the contract does not preclude the third party from enforcing this term. This legislation does not apply to the whole of the UK. However, other jurisdictions have laws with comparable effect and so the position is similar throughout the UK.

Common law will also be relevant to distribution agreements. Particularly pertinent may be provisions relating to termination. Notwithstanding that a contract may have detailed provisions for termination, a party will always have a concurrent common law right to terminate a contract where there has been a sufficiently serious breach of the contract.

The courts can also determine a clause to be unenforceable under the common law rule against penalties. The modern test was set by the Supreme Court in the case of *Cavendish Square Holding BV v Talal El Makdessi* [2015] UKSC 67. The court must first determine whether the clause in question is a primary obligation or a secondary obligation, as the rule does not apply to primary obligations – this a question of substance and not form. Where a clause provides an amount of damages to be paid on breach, the clause will be penal where there is an extravagant disproportion between that sum and the highest level of damages that could possibly arise from the breach. In other cases, where the provision for breach is measured against the interest protected by the contract, the court then assesses whether the remedy is exorbitant or unconscionable. Other relevant factors to the broader assessment include a comparison with damages, whether the parties are advised by lawyers and the extent of negotiations and sophistication of parties.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

There are no restrictions in the UK on the parties' contractual choice of governing law. It is important to establish which law will apply to a contract before the parties enter into any binding agreement and the best way of doing so is to agree at the outset.

A governing law clause allows the parties to specify which law will be used to interpret a contract and deal with any disputes that arise under that contract. The choice of governing law should be considered before a contract is drafted. A lawyer qualified in the relevant jurisdiction will need to advise on how the chosen governing law will apply to the contract. In the absence of an express choice of governing law then, in the event of a dispute, a court will decide which law to apply in accordance with the relevant conflict of laws principles in that jurisdiction.

The Rome Convention

The Rome Convention on the Law Applicable to Contractual Obligations (Rome Convention) governs contracts entered into before 17 December 2009. The Rome Convention sets out the rules for determining the law that should be applied by courts when resolving contractual disputes, but it does not apply to non-contractual obligations. It came into force in 1991.

The Rome Convention applies to any contract where there is no express choice of law. There are special provisions relating to employment and consumer contracts; it does not apply to certain disputes including those involving wills and trusts, property rights related to family relationships, arbitration agreements and disputes governed by company law.

Under the Rome Convention, in the absence of agreement, the contract will be governed by the law of the country with which it is most closely connected. It will be assumed that this is the country where the

party that has to perform the main obligations of the contract is normally resident.

The European Union resolved that the Rome Convention needed to be updated and that its status should change from being a multi-lateral inter-governmental agreement to a Regulation, EC Regulation 593/2008 (Rome I), which applies directly in the laws of the EU Member States and is directly enforceable. Rome I applies to 'contractual obligations in civil and commercial matters'. The term 'contractual obligation' is not defined, and care must be taken about whether a claim is one made in tort (to which Rome II, EC Regulation 864/2007, may apply) or one made in contract. Some claims that are regarded as torts in English law may be regarded as contract claims for the purpose of the two regulations. Contracts entered into on or after 17 December 2009 are therefore governed by Rome I, or the Rome Regulation on the law applicable to contractual obligations. Rome I covers much of the same ground as the Rome Convention and the basic rule has been preserved and firmed up – in the absence of agreement, the applicable law will be the law of the place where the party that has to perform the main obligations of the contract is normally resident. That is now a fixed rule rather than a presumption.

The most important changes brought about by Rome I are as follows.

Specific contract types, such as those dealing with sale of goods, services, franchise arrangements and distribution agreements are addressed. If the contract in question is not one of these, then the governing law will be determined according to 'where the party required to effect the characteristic performance of the contract has his habitual reference', unless it is clear from the circumstances of the case that the law of another country should apply.

In consumer contracts, although the agreement can stipulate which law applies, that cannot invalidate the application of any mandatory rules of law that would otherwise apply to protect the consumer. National courts have some flexibility to decide whether to apply the 'overriding mandatory rules' of another country 'where the obligations arising out of the contract have to be or have been performed', even where the parties have selected another law.

For Rome I to apply, the parties do not need to have an EU connection – all that is required is that the case is raised in a relevant court that raises a choice of law issue in subject matter that falls within the Regulation. The law agreed as the applicable law of the contract does not have to be the law of an EU member state. In non-contractual obligation situations, the general rule in Rome II is that the law of the country in which the damage occurred will be the governing law.

Matters that are expressly excluded from Rome I include revenue, customs and administrative matters; arbitration agreements and agreements on choice of court; issues governed by company law – for example, registration, legal capacity, internal organisation, winding-up or personal liability; obligations arising out of dealings before the contract was finalised.

Choice of a foreign non-EU law will not necessarily prevent the application of mandatory rules of law; a choice of US law will not prevent the application of the Commercial Agency laws protecting agents. In *Ingmar v Eaton Leonard Technologies* [2000] ECR I-9305, the agent was active in the United Kingdom, but the parties had chosen California law to govern the contract. The ECJ held that the mandatory provisions of EU law that are given effect by the UK Commercial Agency Regulations could not be evaded 'by the simple expedient of a choice-of-law clause'. In *Accentuate v Asigra* [2013] EWHC 889 (QB), the English court held it had jurisdiction to hear a claim for compensation under the Agency Regulations, even though the relevant agreement was subject to a choice of Canadian law and arbitration and the Canadian arbitral tribunal had already ruled against the claim.

The UK leaving the European Union may have a significant impact in this area. In the absence of agreement with the EU, there is likely to be uncertainty and significant scope for disputes. However, the choice of English law is likely to be still be upheld by courts in the UK and across the EU post-Brexit. In the EU, the Rome Convention which gives effect to the parties' choice, will continue to apply. Moreover, in March 2018, agreement between the UK government and the EU was reached that most EU law (including the Rome Convention) will continue to apply to the UK during the post-Brexit transition period (30 March 2019 to 31 December 2020).

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

There are no restrictions in the UK on the parties' choice of courts, nor on the choice of arbitration tribunals to resolve contractual disputes except in relation to certain disputes over which certain states may have exclusive jurisdiction such as land, or the constitution of corporate bodies. In the absence of express choice, jurisdiction will be determined either by common law rules or by the European regime that was established to regulate jurisdiction and enforcement of judgments in Europe. As regards disputes subject to the European regime, jurisdiction is governed by the Brussels Regulation (EU) 1215/2012 (known as the Recast Brussels Regulation), which applies to proceedings instituted on or after 10 January 2015 (with the exception of articles 75 and 76, which have applied since 10 January 2014).

If the parties have agreed that the courts of one or more Member States have jurisdiction in relation to a dispute, then the Recast Brussels Regulation recognises that agreement and the agreed courts will have jurisdiction. That jurisdiction will be exclusive 'unless the parties have agreed otherwise' (article 25(1)). This provision applies regardless of where the parties are domiciled and applies even where none of the parties is domiciled in the European Union. So, if two parties domiciled in the United States and China agree that the English courts will have jurisdiction, that will be recognised.

That aside, the default rule is that defendants should be sued in the courts of their domicile (article 4). An exception is that a defendant domiciled in a member state may be sued in another member state:

- in matters relating to a contract, in the courts for the place of performance of the obligation in question; and
- for the purposes of this provision in the sale of goods, the place in a member state where, under the contract, the goods were delivered or should have been delivered and in the case of the provision of services, the place in a member state, where, under the contract, the services were provided or should have been provided (article 7).

In most cases, the place where the services are provided by the distributor will be where the distributor can sue or be sued under a distribution agreement.

In an agency contract, it is the agent who provides the services under the contract. Under the Commercial Agency Directive, a commercial agent has authority to negotiate the sale or purchase of goods on behalf of the principal and, where appropriate, conclude such transactions on behalf of and in the name of that principal. Therefore, the 'place of performance' under article 5 must mean the place of the main provision of those services by the agent. Agents may provide services in several member states. To determine where to sue, a principal should consult the provisions of the agreement; what does it say about where the services are to be provided? If the contract does not help, then the relevant place is where the agent has actually carried out most of his or her contractual activities, assuming the place where the services are mainly carried out is not contrary to the intentions of the parties. If that does not assist then the place should be identified by reference to where the agent is domiciled.

Jurisdiction may be affected by the Hague Convention on Choice of Court Agreements (Hague Convention), which came into force on 1 October 2015 in all EU member states (except Denmark) and Mexico (and Singapore on 1 October 2016). The Hague Convention contains rules regarding the validity and effect of jurisdiction agreements, and the subsequent recognition and enforcement of a judgment given by a court of a contracting state designated in an agreement. It gives effect to an exclusive choice of a court in the contracting state. In essence, the chosen court is obliged to hear the case and any other court must refuse to hear the case. The judgment of the chosen court will be recognised and enforced in other states. The Convention applies to international cases (article 1); a case is international unless the parties are resident in the same contracting state and the relationship of the parties and all other elements relevant to the dispute, regardless of the location of the chosen court, are connected only with that state (article 1(2)).

Although the United States has signed the Hague Convention, this expresses, in principle, only its intention to become a party. It has not yet taken steps to make itself bound.

The common law rules will apply where the European regime does not and where the Hague Convention does not. The common law rules

are based on either service of process (either within or outside the jurisdiction) and submission to the jurisdiction by the defendant.

Parties should take advice from counsel in other jurisdictions to ensure that if proceedings are issued in the courts of that jurisdiction, the foreign court will enforce the jurisdiction clause and either stay proceedings in favour of the UK courts (either Scotland or England and Wales, as applicable), or accept jurisdiction as required. An arbitrator purportedly appointed in Scotland or England automatically has the power to rule on challenges in their jurisdiction.

Practical considerations such as ease of enforcement of any award by an arbitrator will impact upon the choice of arbitration tribunal.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

There are different courts and procedures in the United Kingdom, depending on whether the action is raised in the courts of Scotland or the courts of England and Wales.

Courts

Generally, disputes before the courts of England and Wales are allocated between the county court (claims up to £100,000) and the High Court (claims of more than £100,000).

In Scotland, civil cases can be heard in the applicable Sheriff court (the equivalent of the English county court) or the Court of Session. The Sheriff courts have exclusive jurisdiction over cases with a value up to £100,000.

Procedures

The procedure before the county courts and the High Court in England and Wales is set out in the Civil Procedure Rules 1998 (CPR) as amended from time to time, and supplemented by court-issued guidance.

The procedure before the Court of Session and Sheriff courts in Scotland is set out in the Rules of the Court of Session 1994 (as amended) and the Sheriff Court Ordinary Cause Rules 1993 (as amended) respectively.

Remedies

The remedies most likely to be sought in respect of distribution agreements in the UK are damages (ie, compensation for breach of contract), and specific implement, specific performance or an injunction (ie, an

order compelling a party to comply with its contractual obligations or to prevent a party from carrying out some action). There is no substantial difference in the remedies available in Scotland and England and Wales. However, in Scotland, the innocent party has the option, in addition to the option of accepting there has been a breach and suing for damages, to require implementation of the contract.

Fair treatment

There are no restrictions on foreign businesses using the courts or procedures of Scotland or England and Wales as long as they have jurisdiction. Foreign businesses can expect to be treated fairly and equally. That said, a foreign company may be ordered by an English court to provide security for costs or by a Scottish court to find security for expenses, also known as caution (ie, consign a specified sum with the court pending the outcome of the action). However, such orders are granted relatively rarely.

Disclosure

In England and Wales, parties to proceedings are obliged to disclose at a relatively early stage in the proceedings the documents on which they rely; documents that adversely affect their case; documents that adversely affect another party's case; and the documents that support another party's case, subject to certain exceptions, including the rules on privilege (CPR 31.6). It is also possible for a party to require disclosure of specific documents before proceedings are commenced in certain circumstances. Litigants can request that the court issue a witness summons against an adverse party or third party requiring that witness to attend at court to give evidence or produce documents to the court under CPR 34.2.

In Scotland, there is no obligation of such upfront disclosure as in England and Wales. A party can seek to recover documents by means of a commission and diligence. The court must be persuaded that the documents are relevant to the case and will only grant an order for recovery for specific documents. A party to litigation can seek to recover documentation from an opponent prior to the commencement of an action by seeking an order under section 1 of the Administration of Justice (Scotland) Act 1972. A party to litigation cannot be compelled to provide a witness statement. However, commercial procedures typically require parties to lodge formal witness statements with the court in advance of a proof (hearing on evidence).

Advantages and disadvantages of resolving disputes

The English court system is generally held in high regard internationally due to the independence and impartiality of its judges, the quality of their decision-making and the transparency of the court's procedure. Many foreign companies opt for the jurisdiction of England and Wales for that reason.

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40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

Agreements to mediate will be enforceable in the English and Scottish courts, assuming a bona fide contract has been formed that is subject to the jurisdiction of that court.

An agreement to arbitrate disputes will usually be enforced in England and Wales and recognised under the Arbitration Act 1996. There are requirements for validity such as having been made in writing and relating to a subject matter capable of settlement by arbitration. In addition, there are mandatory provisions that will apply to all arbitrations in England falling within its scope (eg, the provisions of the English Limitation Act 1980). Beyond this, the English regime is permissive and does not contain restrictions on the location or language of the arbitration.

Similarly, there are mandatory rules relating to arbitrations initiated in Scotland. The advantages of resolving disputes by way of arbitration as opposed to through the courts are that arbitration is likely to

be quicker and parties will have more say in who is appointed to preside over the dispute resolution process (eg, an arbitrator with specialist experience in the subject matter of the dispute). In England and Wales, the Arbitration Act 1996 confers upon the English courts powers to make orders in support of arbitral proceedings, such as freezing injunctions or orders for the preservation of documents, for example. London is widely recognised as one of the world's leading international arbitration centres. Numerous arbitral bodies have offices in the city and there is substantial specialist arbitration expertise throughout the legal marketplace. The UK is party to numerous international conventions, such as the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, to facilitate recognition and enforcement of awards made by arbitral tribunals in this jurisdiction. The main disadvantage of resolving disputes by way of arbitration is the limited right of appeal. In addition, while resolving a dispute by arbitration can be quicker, parties will be expected to meet the arbitrator's costs and, as such, it is not necessarily cheaper.

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United States

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Direct distribution

1 May a foreign supplier establish its own entity to import and distribute its products in your jurisdiction?

Generally yes unless the supplier's country, the supplier itself or its principal is the subject of a trade embargo or sanctions. As of December 2018, the countries on the embargo list are the Crimea region of Ukraine, Cuba, Iran, North Korea and Syria. In addition, there are sanctions affecting specified persons and categories of persons relating to the following countries or areas: Afghanistan, the Balkans, Belarus, Burundi, Central African Republic, Democratic Republic of the Congo, Iraq, Lebanon, Libya, Nicaragua, Russia, Somalia, South Sudan, Venezuela, Yemen and Zimbabwe. The lists of embargoed countries and sanctioned individuals and entities are maintained by the Office of Foreign Assets Control (OFAC) of the US Department of Treasury. For details, see the OFAC sanctions page at www.treasury.gov/resource-center/sanctions.

There are also certain industries in which foreign ownership is restricted or regulated, either nationally or by certain states, such as defence contracting, banking and alcoholic beverages.

2 May a foreign supplier be a partial owner with a local company of the importer of its products?

Generally yes, subject to the embargoes, sanctions and certain industries noted in question 1.

3 What types of business entities are best suited for an importer owned by a foreign supplier? How are they formed? What laws govern them?

Any importer, whether foreign-owned or not, should operate through a form of entity whose liability is limited to the assets of the entity, to minimise the risk of the owners' assets being available to satisfy claims for the activities of the business. The most common of these are the corporation and the limited liability company (LLC). These are formed under state law by filing documents with the chosen US state, and that state's laws will govern the entity as to its internal governance and the relationships among the owners and the entity.

While LLCs are generally more flexible with respect to governance, economic structure and corporate formalities, for a foreign parent a corporation will often be preferable from a tax perspective, depending on applicable tax treaties between the United States and the foreign parent's home jurisdiction, as well as the tax laws of that jurisdiction (see question 6).

4 Does your jurisdiction restrict foreign businesses from operating in the jurisdiction, or limit foreign investment in or ownership of domestic business entities?

Generally there are no restrictions, subject to the responses to questions 1 and 2. US states generally do require, if an entity is 'doing business' in the state, that it 'qualify' to do business, which involves a filing with the state, agreement to be subject to jurisdiction of the state, and appointment of an agent for service of legal process in the state. The definition of 'doing business' varies somewhat by state and is extremely fact-based, but generally includes the operation of a business facility in the state. Typically, a company that fails to qualify when it is required to do so will not be entitled to maintain any action or proceeding in the

courts of the state. Of course, there are likely to be tax consequences for a foreign business that operates directly in the United States.

5 May the foreign supplier own an equity interest in the local entity that distributes its products?

See questions 1 and 2.

6 What are the tax considerations for foreign suppliers and for the formation of an importer owned by a foreign supplier? What taxes are applicable to foreign businesses and individuals that operate in your jurisdiction or own interests in local businesses?

Foreign businesses and individuals are generally subject to federal (national US) income tax on their taxable income that is deemed to be 'effectively connected' with a US trade or business ('effectively connected income' or 'ECI') at the normal rates applicable to US persons. Non-US persons must file a US income tax return to report such income and may deduct the expenses of the US business. A foreign corporation that has ECI is subject to an additional 30 per cent US branch profits tax on its after-tax net income. A foreign person is also subject to a 30 per cent US withholding tax on US-source 'fixed or determinable annual or periodic' income, which generally includes dividend income.

If a foreign entity provides services in the US, and those services are performed by employees of the foreign entity, the foreign entity will be engaged in a US business. This means that the foreign entity will have to file a US tax return and report and pay tax on its ECI from those services. Also, if the foreign entity invested in a US operating business directly or through an entity treated as a partnership for US tax purposes, the foreign entity itself would be required to file a US tax return and pay taxes on its share of any ECI generated by the operating business.

In order to alleviate both the implications of having to file a tax return in the US and the payment of the branch profits tax, the foreign entity could establish a US subsidiary corporation to employ the individuals who will perform services in the US or to hold the foreign parent's investment in a US operating business. The US subsidiary would file a US tax return and would be subject to US tax at regular US corporate income tax rates on the income generated by the US business, less its business expenses. If the US subsidiary makes any distributions to the foreign parent during the time that it was operating or holding an investment in a business in the US, the distributions would be subject to a US dividend withholding tax at a rate of 30 per cent (or any lesser rate provided in an applicable income tax treaty between the US and the foreign entity's home country). When the US subsidiary sells its US business or its investment in a US business, the US subsidiary would be subject to US tax on any net gain realised on the sale. However, the US subsidiary could then fully liquidate and distribute the proceeds from its business or its investment to its foreign parent, and that liquidating distribution would not be subject to US withholding taxes. Accordingly, a foreign business or individual can avoid a second level of US tax (ie, branch profits tax or dividend withholding tax) on its US business or its investment in a US business if it makes its investment through a wholly-owned US corporation, and the US corporation does not make any distributions to the foreign parent until it fully liquidates.

However, depending on the tax rules of jurisdiction where the foreign business is located and the structure of the foreign company, it may be preferable to structure the US subsidiary entity as a US partnership

that elects to be treated as a corporation for US tax purposes. This structure will have the same US tax benefits of investment through a US corporation as discussed above and may also allow the investing company or its equity owners to receive a tax credit in its local jurisdiction for the US corporate taxes paid by the US subsidiary. Often income tax treaties between the US and other countries can affect the preferred structure and offer opportunities to reduce the total tax burden from a foreign business's US operations.

Local distributors and commercial agents

7 What distribution structures are available to a supplier?

The options for distribution, for the most part, are limited only by the creativity of the business people structuring the relationship. The most common are discussed below.

Direct distribution

Distribution by the foreign supplier using its own employees or through a subsidiary. See questions 1 to 6.

Commercial agents and sales representatives

The agent does not purchase or take title to the goods, but rather sells them on behalf of the foreign supplier and receives a commission. Matters such as who actually delivers the product, who generates the invoice, how risk of non-payment is shared and other logistical matters may be addressed by contract, together with a definition of each party's duties and how the relationship may be terminated.

Independent distributors

The supplier contracts with an independent distributor that buys goods from the supplier, taking title to those goods, and resells them at a profit to its own customers. The details of the relationship, including the responsibilities of each side and the parties' rights to terminate, are defined by contract.

Franchising

Franchising, under the typical definition, amounts to the use of independent distributors who are licensed to use the supplier's trademarks, either in the business name or in the products sold, are required to follow a prescribed marketing plan or method of operation, and pay a franchise fee to the supplier. The specific definition and the consequences of being deemed a franchise vary from state to state. In many US states, franchises are regulated in one or both of two ways. First, many states and the Federal Trade Commission (FTC) require disclosure documents in a prescribed format to be provided to the prospective franchisee and, in some states, to be registered with the state. Second, some states regulate the substance of the relationship between franchisor and franchisee in various ways, most notably by restricting the franchisor's right to terminate or not renew the relationship except for statutorily defined good cause, often requiring a specified period in which the franchisee may cure any default. States that regulate franchising often require franchisors to submit to jurisdiction and appoint an agent for service of process in the franchisee's state.

Joint ventures

A joint venture can be established by a foreign supplier with its distribution partner in the US, whether the partner is an agent, distributor or franchisee, by having the local distribution entity owned in part by the supplier, directly or through a subsidiary, or through another form of sharing of profits and expenses. An ownership interest can provide greater control through ownership rights and representation on a board of directors or management committee.

Licensing of manufacturing rights

A foreign supplier may license a US manufacturer to use its intellectual property – patent, copyright, trademark or trade secrets – to make its products locally and sell them. While all the implications of licensing intellectual property are beyond the scope of this chapter, care must be taken by the licensor to maintain quality control over the finished product and the use of the intellectual property. Failure to do so can not only put the brand equity at risk, but also risk the loss of trademark protection.

Private label

Distribution of products under a private label amounts to a reverse licensing arrangement, where a US distributor or retailer distributes the foreign supplier's products under the US business's own trademark. In essence, the supplier gives up its own brand name in exchange for the distribution strength of its US partner, with the supplier reaping no enhanced brand value. Control over sales, distribution, marketing and advertising are in the hands of the local brand owner, resulting in negligible distribution costs to the supplier, and virtually no control, save perhaps for sales and performance benchmarks in the contract, with benefits to the supplier limited to its profits on sales of the product.

8 What laws and government agencies regulate the relationship between a supplier and its distributor, agent or other representative? Are there industry self-regulatory constraints or other restrictions that may govern the distribution relationship?

By and large, the relationship between supplier and distribution partner is governed by contract, which the parties are free to structure as they wish. Notable exceptions are: (i) business franchises, which are regulated by federal disclosure requirements and by various state disclosure, registration and relationship laws, discussed briefly in question 7; and (ii) federal and state laws governing certain industries, which can regulate the right of a supplier to terminate a distribution relationship, among other aspects of the relationship. There are federal laws governing automobile dealers and petroleum products retailers (gas stations). Many states have similar laws for those industries, and there are state laws governing beer, wine, spirits, farm equipment and occasionally other industries. (Understanding the laws and regulations governing businesses and individuals in the US is complicated by the fact that there is regulation at the national, federal and state level by each of the 50 US states, Washington, DC, and US territories and possessions, such as Puerto Rico, the US Virgin Islands and Guam.)

Many industries have adopted codes of conduct applicable to companies in the industry, which suppliers often incorporate into their distribution agreements so they become part of the contract. (Some companies incorporate similar codes of conduct that they have adopted individually.) Such incorporated codes of conduct are enforceable just like any other contract provision.

9 Are there any restrictions on a supplier's right to terminate a distribution relationship without cause if permitted by contract? Is any specific cause required to terminate a distribution relationship? Do the answers differ for a decision not to renew the distribution relationship when the contract term expires?

Again, the parties' freedom to contract generally governs the distribution relationship, including the parties' right to terminate or not renew the relationship without cause or for specified reasons. As indicated in question 8, however, some states' laws restrict the ability of franchisors, and of suppliers in certain industries, to end a relationship. Where a statutory restriction exists, it often prohibits termination without 'good cause', 'just cause' or a similar formulation. Such cause is often narrowly defined and typically does not include poor performance, but often does include a material failure to comply with reasonable contractual requirements, which makes clearly drafted and substantively reasonable contractual performance standards important. Moreover, many states require that, before termination occurs, the franchisee or distributor be given a specified period of time – often 60 or 90 days – in which to cure any deficiency or breach. The statutory 'good cause' requirements typically – but not universally – apply equally to a failure to renew a contract on expiry.

In the absence of such a statute, however, there is generally no restriction on the parties' ability to agree on the conditions for termination with or without cause.

10 Is any mandatory compensation or indemnity required to be paid in the event of a termination without cause or otherwise?

When an applicable statute restricts termination without good cause, as discussed in question 9, or where a termination violates a contract's terms, the wrongfully terminated distributor may recover damages, and in some cases may be able to obtain injunctive relief preventing termination. (The requirements for injunctive relief vary from state to

state, but typically require irreparable harm not adequately compensable with money damages. That is often interpreted to mean a likely inability for the business to survive in its current form.) Where damages are to be awarded, the amount will vary from state to state and usually is not defined by any specific formula or multiple of profits or sales. Often the damages will be defined as the fair market value of the distributor's business in the terminated product lines (ie, what a willing buyer and a willing seller, neither under compulsion to deal, would agree on for the price of the business). Damages may also be calculated as the net present value of the profits that would be earned by the distributor in the absence of termination. In the absence of an applicable statute or breach of contract, damages will not be assessed for a proper termination.

11 Will your jurisdiction enforce a distribution contract provision prohibiting the transfer of the distribution rights to the supplier's products, all or part of the ownership of the distributor or agent, or the distributor or agent's business to a third party?

In general, yes. However, as discussed in question 8, there may be specific laws applicable to certain industries that affect the enforceability of such provisions.

Regulation of the distribution relationship

12 Are there limitations on the extent to which your jurisdiction will enforce confidentiality provisions in distribution agreements?

Confidentiality agreements are generally enforced as written, subject to normal contract defences such as fraud or unconscionability, and subject to the obligation to disclose information in legal proceedings and government investigations. US courts have broad disclosure requirements, and the presence of a confidentiality provision will not shield information from discovery if it is material and necessary in the prosecution or defence of an action. While courts disfavour protective orders to maintain the confidentiality of information filed with the court, they can be obtained where necessary to protect competitively valuable information or in other cases where good cause can be shown, particularly where the parties to a litigation can agree, and confidentiality agreements between litigating parties are not unusual to protect sensitive information provided in discovery.

Information disclosed to government agencies may be subject to public disclosure under federal or state freedom of information laws, although there are exceptions, and protection of sensitive information should be discussed with the government prior to disclosure. It is prudent to include in confidentiality agreements a provision calling for advance notice and cooperation from the party being compelled to disclose, to the extent permitted, prior to making a disclosure required by law, so that the party whose sensitive information may be disclosed can seek appropriate protection.

Confidentiality agreements in the US typically exclude from protection information that the receiving party can demonstrate (i) was already known to the receiving party at the time of disclosure, (ii) became public without fault of the receiving party, (iii) is developed independently by the receiving party without reference to confidential information of the disclosing party, or (iv) is learned by the receiving party from a third party not owing any obligation of confidentiality to the disclosing party. Where the information to be protected is not in fact confidential, as in these situations, a court may not enforce the agreement.

Trade secrets – information that is not generally known and provides a competitive advantage to the owner – will be protected from disclosure or misappropriation where the owner has taken appropriate steps to maintain confidentiality, including obtaining written confidentiality agreements from all employees and others to whom the information is disclosed.

13 Are restrictions on the distribution of competing products in distribution agreements enforceable, either during the term of the relationship or afterwards?

In the absence of market power, a supplier generally is free to restrict a distributor's sales of competing products, although some state laws limit this ability. Where exclusive dealing requirements are so broad

as to foreclose a substantial portion of the market, they may be found unlawful as an unreasonable restraint of trade under the antitrust (competition) laws. Restrictions that extend beyond the term of a distribution agreement are disfavoured in some states, and generally must be ancillary to the contract and in furtherance of its lawful purposes, as well as reasonable as to (i) the products restricted, (ii) the geographical scope of the restriction, and (iii) duration. Where a supplier provides a turnkey operation, as in a classic franchise, and discloses all the details of how to operate the business, such post-term restrictions may be more broadly permitted, particularly if they are short in duration and cover a limited geographical area.

14 May a supplier control the prices at which its distribution partner resells its products? If not, how are these restrictions enforced?

In general, US antitrust laws, such as section 1 of the Sherman Act, in the absence of monopoly power, address concerted action, not unilateral conduct. Thus, if the supplier itself is making the sale, as with owned outlets, a controlled subsidiary or, in most jurisdictions, through a true agent, the pricing is unilateral and usually not problematic. But an agreement between independent entities in which the supplier regulates the resale prices of a distributor, franchisee or licensee, raises antitrust concerns. Even in the case of a purported unilateral policy, eg, an announced supplier policy to deal only with retailers that maintain the manufacturer's suggested resale price (MSRP), care must be taken to enforce the policy strictly. Lax enforcement can be construed as coercion of a resale price maintenance agreement rather than mere establishment of a unilateral policy (see question 15).

In 2007, the US Supreme Court held, in *Leegin Creative Leather Products, Inc v PSKS, Inc*, that all vertical agreements (ie, agreements between buyer and seller), even as to resale prices, are judged under federal law by the 'rule of reason', under which the court must determine whether the anticompetitive harm from the conduct is outweighed by potential competitive benefits, rather than by the per se rule, which makes conduct unlawful without regard to any claimed justifications. In *Leegin*, the Supreme Court noted a variety of situations in which resale price maintenance (RPM) may be anticompetitive, and suggested several factors relevant to the rule of reason inquiry, including the number of suppliers using RPM in the industry (the more manufacturers using RPM, the more likely it could facilitate a supplier or dealer cartel), the source of the restraint (if dealers are the impetus for a vertical price restraint, it is more likely to facilitate a dealer cartel or support a dominant, inefficient dealer), and where either the supplier or dealer involved has market power.

Importantly, the states do not always follow federal precedent in enforcing their own antitrust laws and so may not follow *Leegin*. Indeed, some states have antitrust statutes that explicitly bar RPM programmes. Thus, some state authorities will apply the per se rule to RPM under state law. The result is a patchwork of states accepting or rejecting the *Leegin* approach in enforcing state antitrust laws. Consequently, before implementing any RPM programme, counsel must carefully examine each relevant state's treatment of RPM, especially as state law continues to develop, review all the facts, and determine whether any of the factors described by the Supreme Court in *Leegin* are present, or whether there are other indications that the proposed programme will have anticompetitive effects rather than enhancing interbrand competition.

15 May a supplier influence resale prices in other ways, such as suggesting resale prices, establishing a minimum advertised price policy, announcing it will not deal with customers who do not follow its pricing policy, or otherwise?

It is lawful in the US for a supplier to suggest resale prices, so long as there is no enforcement mechanism and the customer remains truly free to set its own prices. In addition, under the rule announced in 1919 by the US Supreme Court in *United States v Colgate & Co*, a supplier may establish a unilateral policy against sales below the supplier's stated resale price levels and unilaterally choose not to do business with those that do not follow that policy, because only agreements on resale pricing may be unlawful. But care must be taken not to take steps that would convert such a unilateral policy into an agreement. When a supplier's actions go beyond mere announcement of a policy and it employs other means to obtain adherence to its resale prices, an RPM agreement can be created. *Colgate* policies can be notoriously difficult

to administer, because salespeople often try to persuade a customer to adhere to the policy, instead of simply terminating sales upon a violation (with the resulting loss of sales to the salesperson), and such efforts can be enough to take the seller out of the *Colgate* safe harbour and into a potentially unlawful RPM situation.

Minimum advertised price (MAP) policies that control the prices a supplier advertises, but not the actual sales price, are also generally permitted, although the issue of what constitutes an advertised price for online sales can have almost metaphysical dimensions. In order to avoid classification as RPM, the MAP policy must not control the actual resale price, but only the advertised price. The closer to the point of sale that advertising is controlled, the greater the risk. Thus, in the bricks and mortar world, policies restricting advertising in broadcast and print media are more likely to be permitted; restrictions on in-store signage would be riskier, and restrictions on actual price tags on merchandise most likely would be deemed a restriction on actual, rather than advertised, price. Online, sellers have most often restricted banner ads and the price shown when an item is displayed, while restrictions on the price shown once a consumer places an item in his or her shopping cart carry a greater risk, which explains why some items are displayed with the legend 'Place item in cart for lower price'. Where the supplier does not prohibit an advertised price inconsistent with the supplier's policy, but instead, as part of a cooperative advertising programme, conditions reimbursement of all or a portion of the cost of an advertisement on compliance with a supplier's MAP policy, the risk is reduced, although not eliminated.

16 May a distribution contract specify that the supplier's price to the distributor will be no higher than its lowest price to other customers?

In general, yes. Such 'most-favoured-customer' clauses are widespread, and courts generally have applied the rule of reason and found that such clauses do not unreasonably restrain trade.

In 2010, however, the US Department of Justice filed an action in federal court in Michigan against health insurer Blue Cross Blue Shield (BCBS), claiming its use of such clauses thwarted competition in violation of antitrust laws. The Department asserted that, because of its market power, BCBS harmed competition by requiring hospitals to agree to charge other insurers as much as 40 per cent more than they charged BCBS. (The case was voluntarily dismissed by the Justice Department after the state of Michigan passed a law prohibiting health insurers from using most-favoured-customer clauses). And in the *Apple Computer e-books* case, a federal district court found that a most-favoured-customer provision in Apple's contracts with publishers that required the publishers to lower the price at which they sold e-books in Apple's store if the books were sold for less elsewhere – notably by Amazon.com – violated the antitrust laws. The decision was affirmed on appeal by the US Court of Appeals for the Second Circuit. Apple sought US Supreme Court review; however, the Court declined to review the decision.

The presence of most-favoured-customer clauses may also lead a supplier to reject an otherwise attractive offer from a customer to take surplus inventory at a lower price, because the discounted price would have to be offered to all customers with a most-favoured-customer clause. Contract drafters should therefore examine whether a most-favoured-customer clause raises antitrust risks in the context of their client's particular market share and pricing practices, with particular caution advisable where market power is present.

17 Are there restrictions on a seller's ability to charge different prices to different customers, based on location, type of customer, quantities purchased, or otherwise?

Yes. The federal Robinson-Patman Act prohibits, with certain exceptions, price differences (as well as discrimination in related services or facilities) in contemporaneous interstate sales of commodities of like grade and quality for use or resale within the US that causes antitrust injury. The basic principle is that big purchasers may not be favoured over small ones. The Robinson-Patman Act also requires promotional programmes to be available to customers on a proportionally equal basis. The Act does not apply to services, leases or export sales.

The statute is often criticised, and is honoured more in the breach than the observance, as quantity discounts are commonplace and government enforcement actions are rare. Private damage actions, however, are still brought with some frequency, although the requirement

of showing antitrust injury is often an obstacle to success. To prevail under the statute, a plaintiff must show that the price difference had a reasonable possibility of causing injury to competition or competitors, a standard that has been tightened by recent case law.

There are two principal defences to a Robinson-Patman Act claim. First, showing that the price difference was justified by cost differences is a defence. This defence, however, is notoriously difficult to establish, requiring detailed data as to the cost differences applicable to the different sales at different prices. Second, under the 'meeting competition' defence, prices may be lowered to meet (but not beat) a competitor's price, where there is a good faith basis for believing the competitor actually made a lower offer. If a copy of the competitor's invoice or price quotation cannot be obtained, the company should gather as much information as possible to support the belief that the competitor offered the lower price. The lower price must not, however, be confirmed with the competitor, which could provide evidence supporting a horizontal price-fixing conspiracy by the suppliers. Rather, the supplier should obtain that information through other sources, such as customer documentation or market surveys.

There are also state laws that restrict price discrimination. Some are generally applicable and modelled on the Robinson-Patman Act, but apply to intrastate sales instead of or in addition to interstate sales. Others restrict 'locality discrimination' – charging different prices in different parts of a state. Some states, such as California, have unfair competition laws that prohibit below-cost pricing (which in certain circumstances may also violate federal law) and the provision of secret and unearned rebates to only some competing buyers. Other state laws apply to specific industries, such as motor vehicles or alcoholic beverages, and prohibit discrimination in pricing to dealers.

18 May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells? Are exclusive territories permitted? May a supplier reserve certain customers to itself? If not, how are the limitations on such conduct enforced? Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

As a general rule, yes. Non-price vertical restraints are judged by the rule of reason in the United States and are generally permitted, in the absence of market power. Customer and territory restrictions, such as exclusive territories pursuant to which a distributor is allocated a specific territory outside of which it may not sell and within which no other distributor may sell the supplier's goods, thus are governed by the rule of reason. Exclusive territories necessarily reduce intrabrand competition between distributors of the same products. But by eliminating one distributor 'free-riding' on the promotional and service efforts of another and undercutting its price, and thus making it feasible for the distributor to sustain those efforts, exclusive territories enhance interbrand competition between suppliers of competing products, and so are generally viewed as pro-competitive on balance.

The distinction between active and passive selling applicable in Europe is not generally relevant under US antitrust law. Another distinction from the European approach is that restrictions on online sales are viewed as a non-price vertical restraint, and so are judged by the rule of reason and generally permitted, in the absence of market power. Courts have upheld prohibitions on mail order and telephone sales under the rule of reason, and restrictions on internet sales – even an absolute prohibition – should be judged no differently.

However, customer allocation by competitors is a horizontal arrangement rather than a vertical one and is per se illegal. It is thus critical that the impetus for exclusive territories come from the supplier in a vertical arrangement and not from dealers or distributors making a horizontal allocation of territories.

Many US cases apply a 'market power screen' in rule of reason cases, and uphold non-price vertical restraints whenever the defendant lacks market power. Such restraints, including exclusive territories, will be viewed more sceptically if market power exists.

19 May a supplier restrict or prohibit e-commerce sales by its distribution partners?

As noted in response to question 18, restrictions on online sales are a non-price vertical restraint, judged by the rule of reason and generally permitted, in the absence of market power. Courts have upheld

prohibitions on mail order and telephone sales under the rule of reason, and restrictions on internet sales – even an absolute prohibition – should be judged no differently.

The inherently borderless nature of e-commerce means that e-commerce sales, if permitted or secondarily sourced, may well adversely affect distributors into whose exclusive territories e-commerce sales are made, and may benefit distributors who have distribution centres of e-commerce intermediaries located in their territories from which sales are made to the territories of other distributors. These disproportionate effects may be dealt with in the contract by having the distributor that benefits from out-of-territory sales by an intermediary in its territory pay over an ‘invasion fee’ or similar payment to the distributor into whose territory the sales are made. Of course, this requires a determination of the number of ‘transferred’ sales made by the intermediary. If reporting of such sales can be obtained, of course, that determination is easy. Otherwise, some kind of estimate is needed, perhaps based on relative non-e-commerce sales volumes in the territories. Again, though the fundamental freedom to contract applies, and such determinations are permitted and becoming more common.

20 Under what circumstances may a supplier refuse to deal with particular customers? May a supplier restrict its distributor's ability to deal with particular customers?

In general, a business that does not have market power is free to choose its customers and do business or not do business with whomever it wishes. That can include restricting a distributor's ability to do business with particular customers or classes of customers, a vertical restraint that will be judged by the rule of reason, as discussed in questions 14 and 18. A supplier with market power will be more limited in its ability to engage in such practices, if an adverse effect on competition can be shown. In certain circumstances, courts have found that a monopolist may have an obligation to deal, or to continue dealing, with its competitors.

Note that an agreement among competitors at the same level of distribution not to deal with certain customers, or to restrict with whom customers may deal, will be treated as a horizontal, per se illegal restraint, rather than as a vertical restraint governed by the rule of reason. Thus where a restriction on dealing with certain customers originates with a group of competing distributors, a supplier may be at risk of being found to be an illegal participant in that horizontal conspiracy, where the same restraint originated by the supplier might well be lawful.

There may be some industries in some states where a supplier is required to deal with all customers. For example, in many states, alcoholic beverage wholesalers must sell to all licensed retailers.

21 Under which circumstances might a distribution or agency agreement be deemed a reportable transaction under merger control rules and require clearance by the competition authority? What standards would be used to evaluate such a transaction?

Acquisitions of businesses or interests in businesses, including a supplier's purchase of an ownership interest in a distributor, may be subject to filing requirements and federal antitrust agency review if certain thresholds are met as to the size of the transaction (more than US\$84.4 million) and the size of the parties (if the value of a proposed transaction is more than US\$ 337.6 million, it is reportable; if the value is more than US\$84.4 million but less than US\$337.6 million, it is reportable if one party to the transaction has total assets or net sales of US\$ 168.8 million or more and the other has total assets or net sales of US\$16.9 million or more). The above dollar amounts are adjusted annually for inflation. New dollar thresholds are expected to be announced in early 2019. In the absence of an ownership interest, however, distribution relationships are not generally subject to antitrust reporting requirements or agency clearance procedures.

22 Do your jurisdiction's antitrust or competition laws constrain the relationship between suppliers and their distribution partners in any other ways? How are any such laws enforced and by which agencies? Can private parties bring actions under antitrust or competition laws? What remedies are available?

As discussed in questions 14 and 18, vertical agreements between suppliers and distributors are generally governed by the rule of reason,

under which the anticompetitive effects of the restraint are weighed against any possible pro-competitive effects, and in the absence of market power, will usually be found lawful. In contrast, horizontal agreements among competitors at the same level of distribution relating to matters such as pricing, allocation of customers or territories, or production levels, are prohibited by the per se rule.

Accordingly, it is important for suppliers and distributors not only to avoid such agreements with their competitors, but also to avoid putting themselves or their distribution partners into a position where they might be deemed participants in a horizontal conspiracy at either distribution partner's level of distribution. Thus, suppliers should not exchange current or future pricing or production information with their competitors, should not use their common distributors to facilitate such information exchanges, should not share one distributor's pricing information with other distributors, and should not agree to territorial allocations made by their distributors rather than imposed by the supplier. Distributors should not share with one supplier pricing or production information received from another. Similarly, suppliers should not share information with each other about their common distributors, as such exchanges could support a claim of a concerted refusal to deal should both suppliers then decide to terminate their relationships with the distributor.

Returning to purely vertical relationships, a supplier may not require its customers to purchase one product (the tied product) in order to be able to purchase another product (the tying product), if the supplier has substantial economic power in the tying product market and a ‘not insubstantial’ amount of interstate or international commerce in the tied product is affected. One of the difficult questions in a tying analysis is whether there are in fact two distinct products, one of which is forced on customers who would not otherwise purchase it as a result of market power with respect to the other.

The antitrust laws are enforced both by government action and by private party litigation. At the federal level, both the US Department of Justice and the FTC enforce the antitrust laws. They may seek criminal or civil enforcement penalties. Jail terms are not uncommon for antitrust violations, especially horizontal ones. Maximum fines for each violation are US\$1 million for individuals and US\$100 million for corporations, subject to being increased to twice the amount gained from the illegal acts or twice the money lost by the victims of the crime, if either of those amounts is over US\$100 million. In addition, both federal agencies can bring civil actions to enjoin violations of the antitrust laws, disgorge profits, impose structural remedies and recover substantial civil penalties. The federal agencies often cooperate with foreign antitrust and competition authorities in investigating violations.

State attorneys general also actively prosecute antitrust cases and have similar authority to the federal agencies within their own states. State antitrust laws also provide civil and criminal penalties, and the states frequently cooperate with each other and with the federal agencies in multistate investigations and prosecutions.

Last, but certainly not least, private plaintiffs may bring civil actions under the antitrust laws and recover treble damages – that is, three times the actual damages caused by the violation – and attorneys' fees (not the usual rule in the US, where each party generally pays its own legal fees, regardless of who prevails). The exposure in an antitrust action can thus be extremely high, as can the costs of litigation.

23 Are there ways in which a distributor or agent can prevent parallel or ‘grey market’ imports into its territory of the supplier's products?

Importation of goods bearing a registered trademark, even if genuine, can be blocked through the US Customs and Border Protection Service (CBP), provided the non-US manufacturer is not affiliated with the US trademark owner, under the Tariff Act, which prohibits the importation of a product manufactured abroad ‘that bears a trademark owned by a citizen of . . . the United States’. The CBP can also block genuine trademarked goods not intended for the US market, even if the non-US manufacturer is affiliated, if the goods are physically and materially different from the goods intended for sale in the US. However, the grey importer can bring in the products if a disclaimer is affixed stating that the goods are materially and physically different from the authorised US goods. In addition, where parallel imported goods are materially different from the US goods in quality, features, warranty or the like, a trademark infringement claim is possible where customer confusion is likely.

There is no current ability to restrict grey market importation under a copyright theory. The Supreme Court held in 2013, in *Kirtsaeng v John Wiley & Sons Inc*, that a copyright owner cannot exercise control over a copyrighted work after its first sale, even if that first sale occurs outside the US. Moreover, reliance on an insubstantial element of a product protected by copyright to attempt to block parallel imports may be held to be copyright misuse, which prevents enforcement of the copyright.

Until recently, grey market importation of products protected by a US patent infringed the patent even if the products were lawfully sold abroad with the authority of the patent holder. However, in 2017, the US Supreme Court held in *Impression Prods, Inc v Lexmark Int'l, Inc* that an authorised sale abroad of a product protected by a US patent exhausted the patentee's right to prevent importation into the United States. Accordingly, patent law has been changed to conform to copyright law, as discussed above.

24 What restrictions exist on the ability of a supplier or distributor to advertise and market the products it sells? May a supplier pass all or part of its cost of advertising on to its distribution partners or share in its cost of advertising?

Advertising is regulated by both federal and state laws that prohibit false, misleading or deceptive advertising. Where advertising makes statements that could reasonably be interpreted as an objective factual claim (in contrast to statements such as 'world's best water', that are more likely to be regarded as marketing puff), the advertiser must have reasonable substantiating documentation to support the claim before the advertising is disseminated.

Federally, advertising is regulated principally by the FTC. The FTC has broad authority under the FTC Act to prevent 'unfair or deceptive acts or practices' and more specific authority to prohibit misleading claims for food, drugs, devices, services and cosmetics. The FTC can sue in the federal courts, and often will enter into consent orders with defendants in advance of litigation that may incorporate a variety of remedies.

The FTC considers advertising deceptive if it contains misrepresentations or omissions likely to mislead consumers acting reasonably to their detriment. While the FTC must show the deception was material to consumers' purchasing decisions, it does not have to show actual injury to consumers. Similarly, the FTC deems advertising to be unfair if it causes or is likely to cause substantial consumer injury that is not reasonably avoidable by consumers themselves and is not outweighed by countervailing benefits to consumers or competition.

The most common remedy in advertising cases is an order to enjoin the conduct complained of and prevent future violations. Where such an order is not enough to correct misunderstandings caused by misleading advertising, the FTC may order corrective advertising. In addition, the FTC may seek other consumer redress or disgorgement of profits, and, in the case of violations of prior orders or trade regulation rules, civil penalties.

The states regulate advertising in similar ways under a variety of state unfair competition and unfair trade practice statutes. These are enforced by the state attorneys general in a manner similar to the FTC.

Finally, private parties – often competitors – can bring actions in the state and federal courts to enjoin or seek damages for false or deceptive advertising that causes harm to competitors or consumers.

There are additional restrictions on specific types of advertising. Sweepstakes, in which prizes are awarded by chance to consumers who have made a purchase or provided some other consideration, are regulated by many states, some of which require prior registration. Endorsements are regulated, most notably by the FTC Endorsement Guidelines, which are intended to ensure that statements of third-party endorsers reflect an honest statement of the endorser's opinion and are substantiated to the same extent as required for the advertiser's own statements. The Guidelines require, among other things, disclosure of any relationship between the endorser and the supplier of the product, including requiring the supplier to ensure that bloggers who review a product disclose when the supplier provided a free sample for evaluation and that employees who comment on their employer's products or services on social media or websites disclose that relationship.

Finally, there are specific regulations governing certain claims, such as those asserting health benefits, or claiming 'green' products, and many industries have adopted self-regulatory advertising codes that should be followed.

There are no restrictions on suppliers requiring reimbursement or contributions for advertising costs from distribution partners, or on distribution partners agreeing to share in the advertising expenses. Freedom of contract governs, and it is commonplace to include provisions governing the sharing of advertising costs or the contribution from each party to advertising funds to support the products being distributed.

25 How may a supplier safeguard its intellectual property from infringement by its distribution partners and by third parties? Are technology-transfer agreements common?

Trademarks

Trademarks receive some protection by virtue of use in the US under the federal Lanham Act and under the common law of the states where they are used. The preferable, more effective way to protect trademarks in the US is to obtain trademark registrations through the US Patent and Trademark Office. US trademark registrations can be based on a supplier's home country trademark registration or on use in interstate or foreign commerce in the US. Applications can also be based on an intent to use the trademark in the US, but the registration will not be issued until the supplier has submitted proof of actual use in the US. US federal trademark registration can also be obtained under the Madrid Protocol if the supplier's home country is a signatory to the treaty.

Only the owner of a trademark may obtain a US registration. Accordingly, in general the supplier, not the local distributor, will be the applicant. Contracts typically forbid the distributor from registering the trademark to protect the supplier from infringement by its distribution partner.

Patents

In general, patent protection in the US must be sought in conjunction with patent protection in the supplier's home country. If a US patent application has not been filed within a specified period of time – usually one year – after the home country filing, a US patent will not be available. A longer period may apply under the Patent Cooperation Treaty if the home country is a signatory.

Assuming there is US patent protection, the supplier may enforce the patent through private lawsuits in US courts against infringers. Both injunctive relief and damages are available remedies. Where the infringing goods are imported into the US, an exclusion order from the International Trade Commission may also be sought. While this procedure is faster, no damage remedy is available. Unauthorised sale of patented products by the distribution partner is usually regulated by contract but can also be remedied through an infringement suit.

Copyright

Under the US Copyright Act, the copyright in a work of authorship, including textual, artistic, musical and audio-visual works, is protected from the moment the work is fixed in a tangible medium of expression. Publication with a copyright notice is no longer necessary to retain US copyright protection. However, a supplier's ability to protect its copyrights in the US is significantly enhanced by registration with the US Copyright Office. First, registration is required before a copyright can be enforced in the US courts. (Court decisions are currently in conflict as to whether submission of an application for registration satisfies this requirement or whether the registration must actually have been issued. The US Supreme Court is likely to resolve this conflict in 2019, when it decides the case of *Fourth Estate Public Benefit Corp v Wall-Street.com, LLC*.) Second, where a copyright has been registered before an infringer's activities began, the remedies available for infringement are enhanced: the plaintiff need not prove actual damages from the infringement, but may elect to recover 'statutory damages' in an amount, to be set by the court or jury, of up to US\$150,000 per infringed work in the case of wilful infringement. In addition, where the copyright is registered, the plaintiff may recover, at the court's discretion, the costs of the suit including attorneys' fees.

Trade secrets and know-how

See question 12 concerning protection of trade secrets as against distribution partners. Third parties who steal trade secrets (eg, by industrial espionage or hiring of key employees) may be sued for theft of trade secrets under applicable state or federal law. For employees, mere knowledge in a particular field acquired through long experience with

one employer is not a protectable trade secret that will prevent a key employee from changing jobs. In such circumstances non-compete agreements may give suppliers some protection, but there are limits on the time frame and geographical scope.

Technology-transfer agreements

Technology-transfer agreements are typically used to transfer technology from development organisations, such as universities or government, to commercial organisations for monetisation. They are not commonly used to structure the relationships between commercial suppliers and their distribution partners, where a licence agreement is more common.

26 What consumer protection laws are relevant to a supplier or distributor?

There are many federal and state consumer protection laws that are important to suppliers and distributors, well beyond what can be addressed in any detail here. At the federal level, these include a number of laws relating to consumer credit, including the Fair Credit Reporting Act, Truth in Lending Act, Fair Credit Billing Act, Fair Debt Collection Practices Act, Identity Theft and Assumption Deterrence Act of 1998 and Credit Accountability, Responsibility, and Disclosure Act. Other federal consumer protection laws and regulations include the CAN-SPAM Act (regulating the use of unsolicited commercial email), FTC Used Car Rule, FTC Mail or Telephone Order Merchandise Rule (which covers internet and fax sales as well as telephone and mail order sales and regulates shipment times and related statements and cancellation rights), FTC Telemarketing Sales Rule under the Telemarketing and Consumer Fraud and Abuse Prevention Act, and various labelling and packaging requirements for food and beverages, textiles and wool, appliances, alcoholic beverages and other industries. To gain a sense of the range of regulations and to review FTC guidance on the subject, visit the FTC website at www.business.ftc.gov.

In addition, most states have very broad consumer protection laws governing unfair or deceptive trade practices and specific laws governing industries such as mobile homes, health clubs, household storage, gasoline stations and others. Often these provide a consumer right to rescind contracts made in certain circumstances within a defined period. For example, in New York, there is a 72-hour right to cancel for door-to-door sales, dating services, health clubs and home improvement contracts. Contracts for such transactions must clearly state the right to cancel.

See also questions 24 and 28 regarding advertising and warranties.

27 Briefly describe any legal requirements regarding recalls of distributed products. May the distribution agreement delineate which party is responsible for carrying out and absorbing the cost of a recall?

Recalls of products are regulated by a number of federal and state agencies, including the Food and Drug Administration, the US Department of Agriculture and the Consumer Product Safety Commission. In addition, manufacturers, importers and distributors often initiate voluntary recalls to remove a defective or dangerous product from the marketplace before it can cause harm, so as to avoid the potential liability and reputational harm that can come from damage, injuries or deaths.

It is prudent to define in the distribution contract the parties' respective responsibilities in the event of a recall, including who may decide to initiate a recall, how it will be implemented and who will pay the costs, including credits that direct and indirect customers may require for recalled products.

28 To what extent may a supplier limit the warranties it provides to its distribution partners and to what extent can both limit the warranties provided to their downstream customers?

There are both federal and state laws regulating warranties. The main federal law is the Magnuson-Moss Warranty Act, which applies to consumer products with a written warranty. While there is no requirement that a warranty be offered, if a written warranty is provided, then the Act requires certain disclosure of warranty terms, imposes certain requirements, and mandates certain remedies for consumers.

The Act and FTC Rules under it require that a written warranty be stated to be either 'full' or 'limited' for any consumer product that costs more than US\$10, and imposes disclosure requirements for products

costing more than US\$15. Specified information about the coverage of the warranty must be set forth in a single document in simple, readily understood language, and the warranties must be available where the products are sold so that consumers can read them before deciding to purchase.

A warranty is 'full' only if (i) it does not limit the duration of implied warranties (discussed below); (ii) warranty service is provided to anyone who owns the product during the warranty period, not just the first purchaser; (iii) warranty service is provided free, including costs of returning, removing and reinstalling the product; (iv) the consumer may choose either a replacement or a full refund if the product cannot be repaired after a reasonable number of attempts; and (v) consumers are not required to do anything as a condition to obtain warranty service (including returning a warranty card), other than to give notice that the product needs service, unless the requirement is reasonable. If any of these conditions is not met, then the warranty is limited rather than full.

The FTC requires disclosure of certain elements in every warranty, including precisely what is and is not covered by the warranty, when the warranty begins and ends, how covered problems will be resolved and, if necessary for clarity, what will not be done or covered (eg, shipping, removal or reinstallation costs, consequential damage caused by a defect, incidental costs incurred), and a statement that the warranty 'gives you specific legal rights, and you may also have other rights which vary from state to state'. Any additional requirements or restrictions, such as acts that will void the warranty, must be disclosed.

The Magnuson-Moss Act prohibits a written warranty from disclaiming or modifying any warranties that are implied under applicable law, as discussed further below, although a limited warranty may limit the duration of implied warranties to the duration of the limited warranty, subject to contrary state law.

A written warranty cannot be conditioned on the consumer product being used only with specific other products or services, such as particular accessories, but it may provide that it is voided by the use of inappropriate replacement parts or improper repairs or maintenance. A waiver can be obtained from the FTC if it can be shown that a product will not work properly unless specified parts, accessories or service are used.

The FTC, the Department of Justice and consumers can sue to enforce the Act, and consumers can recover their court costs and reasonable attorneys' fees if successful. The Act also encourages businesses to establish informal dispute resolution procedures to settle warranty disputes. Such procedures must meet certain requirements, and must be non-binding on the consumer.

In addition, other federal laws and regulations govern such topics as warranties for consumer leases, used cars and emissions control systems and advertising of warranties.

In almost all states, warranties are governed by the Uniform Commercial Code, which provides for an express warranty, an implied warranty of merchantability and an implied warranty of fitness for a particular purpose. The implied warranty of merchantability is an implied promise, whenever the product is sold by a merchant, that the goods will function properly for the ordinary purposes for which they are used, would pass without objection in the trade, are adequately packaged and labelled, and conform to any promises made in labelling or packaging. The implied warranty of fitness for a particular use exists only when the seller has reason to know the purpose the buyer intends to use the product for at the time it is sold and the buyer relies on the greater knowledge and recommendation of the seller in selecting the product.

The extent to which implied warranties may be disclaimed varies by state. Where permitted, disclaimers usually must be conspicuous, usually interpreted as boldface capital letters. Similarly, state law may permit sellers to limit the damages and other remedies available in case of a breach of warranty. Notice of such disclaimers also generally must be conspicuous.

Many states also have specific 'lemon laws' governing motor vehicles.

29 Are there restrictions on the exchange of information between a supplier and its distribution partners about the customers and end users of their products? Who owns such information and what data protection or privacy regulations are applicable?

In contrast to many other countries, federal privacy regulation in the United States is limited to a few specific areas, such as children's

information, healthcare, financial services and telecommunications. The primary federal regulatory focus is on matters such as transparency to the consumer with respect to the manner in which information will be used and shared and the reasonableness of the data security protections in place. The FTC and other federal agencies have adopted rules in these areas, generally requiring notice to consumers about collection and use of information; consumer choice with respect to the use and dissemination of information collected from or about them; consumer access to information about them; and appropriate steps to maintain the security and integrity of any information collected. The FTC and state regulatory authorities have also been active in regulating behavioural advertising, mobile apps and information security, and businesses gathering customer information should familiarise themselves with the FTC's guidance in these areas.

Until 2015, companies in the US could subscribe to the Safe Harbour principles agreed to between the FTC and the EU, thereby bridging the gap between EU privacy principles and those of the US, and permitting EU businesses to exchange personal data with their US affiliates and business partners, including distribution partners. The October 2015 decision of the European Court of Justice in the *Schrems* case invalidated the Safe Harbour arrangement and called into question the ability to share data between the EU and the US in the absence of Binding Corporate Rules, standard contract clauses or some other permitted undertaking of compliance with EU data protection rules. Negotiations to replace the Safe Harbour regime led to a replacement arrangement adopted in 2016 called the EU-US Privacy Shield, which imposes more robust and detailed data protection obligations on US companies that subscribe, including annual self-certification to their compliance with the principles of the Privacy Shield. The Privacy Shield offers EU citizens several routes to redress: complaints to the company must be resolved within 45 days; a no-cost alternative dispute resolution mechanism will be available; and complaints may be made to local European data protection authorities, which will then work with the US Department of Commerce or FTC to make sure that complaints are investigated and resolved. The future viability of the Privacy Shield has been seriously questioned in light of the *Schrems* decision, and a provision for annual review of the effectiveness of the Privacy Shield calls into question the extent to which US companies may rely on it. As an alternative to the Privacy Shield, parties to EU-US distribution relationships may rely on binding corporate rules (which are expressly permitted under the European Union's General Data Protection Regulation) or on standard contractual clauses that have been approved by the European Commission (which remains a permitted mechanism to transfer personal data outside the European Union, at least for now).

In general, companies collecting information about consumers must say what they will do with the collected information, and do what they say. Within that construct, and subject to the specifically regulated areas, suppliers may exchange customer information with their distribution partners freely, so long as adequate notice of that information exchange has been provided to consumers.

Beyond federal law, all US states and most US territories have also adopted legislation governing consumer information, with data breach legislation imposing notification obligations and remedial action in the event of a security breach being the most common. These state requirements sometimes conflict, which can create problems. A number of states impose specific security obligations on businesses that collect consumer information. For example, the California Consumer Privacy Act of 2018 is a comprehensive data privacy law that will impact businesses around the world that obtain, use, store or otherwise process the personal information of California residents (including California residents who are temporarily located in other places). Among other things, this law would provide California residents the right to know what personal information is being collected about them, the right to know whether their personal information is sold or disclosed and to whom, and the right to say no to the sale of personal information. This law is scheduled to become effective in 2020, though amendments to the law have been made since it was enacted, and future amendments are likely.

In addition, the European Union's General Data Protection Regulation (GDPR), which took effect in May 2018, applies to parties in the United States that (i) offer goods or services (even for free) to individuals in the European Economic Area and (ii) process personal data

of individuals in the European Economic Area in connection with that activity. The GDPR's definition of 'personal data' is very expansive, and provides that a wide range of personal identifiers (eg, IP addresses) constitutes personal data. The GDPR gives individuals in the European Union greater control over their personal data and imposes many new obligations on organisations that collect, handle and otherwise process personal data. The GDPR also gives national data protection authorities the power to impose significant fines on organisations that fail to comply.

Parties should clearly define in their distribution contract who owns the customer information that has been collected, who has access to it, who has the right to determine the purposes and means of processing of that information and the applicable confidentiality obligations (which must conform to the parties' respective stated privacy policies, which in turn must be consistent with each other). In the absence of such a definition, customer data is likely to belong to the party that collected it, but the sharing of such information without a statement of the recipient's obligations may result in the recipient's ability to do as it wishes with the information. Suppliers and their distribution partners also should cooperate in planning to prevent security breaches, and to respond to them in accordance with applicable law when they occur.

30 May a supplier approve or reject the individuals who manage the distribution partner's business, or terminate the relationship if not satisfied with the management?

Under the general principle of freedom of contract, the parties generally may provide as they wish with respect to supplier control over the persons who manage the distributor. Thus, the contract can grant authority to a supplier to approve or reject the individuals who manage the distribution partner's business or the distribution of the supplier's products specifically, as well as to terminate the agreement if not satisfied. And again, this general principle is subject to specific franchise or industry regulation, as discussed in questions 8 and 9. Particularly for alcoholic beverages, many states have laws designed to protect the independence of wholesale distributors; in such states provisions giving suppliers control over distributor management may be problematic and unenforceable. And where termination is limited to statutorily defined good cause as addressed in questions 8 and 9, a right to terminate for dissatisfaction with management may be unenforceable.

31 Are there circumstances under which a distributor or agent would be treated as an employee of the supplier, and what are the consequences of such treatment? How can a supplier protect against responsibility for potential violations of labour and employment laws by its distribution partners?

There is a risk that distributors – especially single-employee companies or sole proprietorships – might be deemed employees of the supplier. To prevent this, it is in the supplier's interest to ensure an independent contractor relationship between itself and the distributor.

The tests for distinguishing bona fide independent contractors from employees vary from state to state, agency to agency, and statute to statute, but they generally weigh various factors, including:

- Does the distributor perform work for other clients and market its services to the general public, or does it work exclusively for the supplier?
- Has the distributor made substantial investments in its own vehicles or other equipment or does the distributor rely on equipment of the supplier?
- May the distributor hire its own employees to perform services for the supplier?
- Does the distributor control its schedule and how it accomplishes its work or is it subject to the supplier's instructions?
- Is the parties' relationship limited in duration or open-ended?
- Does the distributor have substantial skills, experience and training, or is supplier training required?
- Are the distributor's services similar to those of the supplier's employees?
- Does the distributor earn a profit or risk a loss on resales or receive a sales commission or other compensation for its results, or is it compensated for its time (eg, on an hourly or salary basis)?
- Does the distributor receive employee-type benefits from the supplier (eg, vacation days, sick pay, health insurance)?

No single factor is dispositive – the determination is made on the totality of circumstances based on the facts of each case. The distribution agreement, while not dispositive, should state the parties' intent.

Misclassification may result in substantial employment and tax liabilities for the supplier, including retroactive pay and benefits, other damages and substantial fines and penalties. Employees are generally entitled, among other benefits, to minimum wage and overtime compensation, discrimination and workplace safety protections, unemployment benefits, workers' compensation and disability insurance, protected family, medical and military leaves of absence, and a right to participate in the employer's retirement and health plans and other benefits. While there are federal employee rights, specific benefits vary from state to state.

Suppliers should engage experienced employment counsel to analyse the relevant facts and determine the proper classification.

There is also a risk that a supplier could be deemed a joint-employer of an individual employed by a distributor, rendering the supplier liable for compliance with statutory obligations to the employee, such as minimum wage or overtime, benefits and protection against harassment. Factors that are looked at to determine whether a supplier is the joint employer of a distributor's employee include (i) whether the supplier regularly controls the employee's schedule or workload, benefits from the individual's services, supervises the employee, or has any overlapping owners, officers or managers with the distributor, and (ii) whether the employee is economically dependent on both the supplier and the distributor (eg, whether the supplier has the power to hire or fire the employee, or the power to change any of the employee's terms of employment), and how long the distributor's employee has performed the services for the supplier.

32 Is the payment of commission to a commercial agent regulated?

About half the US states have laws regulating commission sales representatives. These laws typically require written agreements setting forth how commission is calculated and require payment within a specified period after termination. Some laws provide for double or treble damages for violations. A few, such as Puerto Rico and Minnesota, restrict a supplier's right to terminate a sales representative without statutory 'good' or 'just' cause. In some states, sales representatives may also be protected by franchise laws in certain circumstances. See questions 8 and 9.

33 What good faith and fair dealing requirements apply to distribution relationships?

A covenant of good faith and fair dealing is implied by the laws of most states in all commercial contracts, including distribution agreements. This requires the parties to deal with each other in good faith, but generally does not supersede express contractual provisions. Thus, a complaint that a supplier terminated a distribution contract in bad faith, in violation of the covenant of good faith and fair dealing, will generally not succeed in the face of a contractual provision allowing the supplier to terminate without cause. Indeed, cases in a number of states hold that a claim cannot be based solely on a breach of the implied covenant of good faith without some breach of an express provision as well.

In contrast, other courts have found a violation of the implied covenant of good faith where suppliers have acted to the disadvantage of their dealers, notwithstanding an express provision permitting the conduct at issue. For example, a federal district court found that sales by the Carvel ice cream company to supermarkets might violate its duty of good faith to its franchisees, notwithstanding its contractually reserved right, in its 'sole and absolute discretion', to sell in the franchisees' territory via the same or different distribution channels.

Similarly, some courts have found a violation of the implied covenant of good faith where the manner in which a supplier exercised its contractual rights demonstrated bad faith, such as disparagement of the distributor or misappropriation of confidential customer information in connection with an otherwise permitted termination.

Moreover, some of the specific industry laws discussed in questions 8 and 9 impose an explicit obligation of good faith on suppliers and distributors that may be independently enforceable.

34 Are there laws requiring that distribution agreements or intellectual property licence agreements be registered with or approved by any government agency?

With the exception of those state franchise laws that require registration of disclosure documents, as discussed in question 7, and some state laws governing specific industries, such as alcoholic beverages, there generally are no such requirements.

35 To what extent are anti-bribery or anti-corruption laws applicable to relationships between suppliers and their distribution partners?

In addition, it is important that counsel for multinational businesses recognise the risks to a supplier of third-party misconduct by foreign distributors and agents under the Foreign Corrupt Practices Act (FCPA). The FCPA, a criminal statute, prohibits bribery of foreign officials, political parties and candidates for public office. Under the FCPA, a company or individual can be held directly responsible for bribes paid by a third party if the company or individual has knowledge of the third party's misconduct. For example, the FCPA prohibits the giving of anything of value to 'any person' while knowing that all or a portion of such money or thing will be given, 'directly or indirectly', to bribe any foreign official, foreign political party or official, or to any candidate for foreign political office. Moreover, constructive knowledge of the misconduct, including wilful blindness or deliberate ignorance, is enough to impose liability. A defendant may be convicted under the FCPA based upon the defendant's 'conscious avoidance' of learning about a third party's illegal business practices. Accordingly, it is critically important to take steps to prevent such misconduct by those acting on a business's behalf, including distributors, agents, brokers, sales representatives, consultants, advisers and other local business partners. A business with foreign business partners must exercise appropriate due diligence in selecting its partners, and adequately supervise their activities. It is important to consider FCPA compliance before entering into an agreement with a foreign partner through due diligence, in the agreement through provisions requiring FCPA compliance and reporting, and after entering into the agreement through ongoing training, monitoring and audits.

36 Are there any other restrictions on provisions in distribution contracts or limitations on their enforceability? Are there any mandatory provisions? Are there any provisions that local law will deem included even if absent?

Except for the specific industry regulation and franchises, discussed in questions 8 and 9, and the antitrust restrictions discussed throughout this chapter, the parties are generally free to structure their relationship as they wish. Of course, distribution contracts are subject to the usual contract enforceability defences, such as fraud, unconscionability, lack of consideration and the like. As discussed in questions 26 and 31, there are certain warranties and a covenant of good faith and fair dealing implied by law; laws governing specific industries and franchises may impute or require other provisions.

In addition, if the contract gives a supplier effective control over the distributor's operations, it may be held vicariously liable to third parties for the distributor's negligence or other misconduct. Similarly, a supplier may be liable for conduct of a distributor that is required by the supplier or represented as part of the supplier's operations.

Governing law and choice of forum

37 Are there restrictions on the parties' contractual choice of a country's law to govern a distribution contract?

A choice of law provision in the distribution contract selecting the law of a specific state or country may be enforced, if the jurisdiction chosen bears a reasonable relationship to the transaction (eg, the supplier's or distributor's home jurisdiction). Such contractual choice of law provisions, while generally enforced, is sometimes disregarded by courts in deference to the public policy of states with business franchise or protective industry laws of the sort discussed in questions 8 and 9, or because the validity of the contract containing the clause was questioned. And courts have refused to enforce choice of law provisions that bear no reasonable relation to the parties or contract.

In selecting a particular state's law, note that this may result in the application of either a more or less restrictive state franchise law than might otherwise be the case.

Combining a choice of favourable law with an arbitration clause will enhance the likelihood of the choice of law being enforced. The strong federal policy in favour of arbitration, embodied in the Federal Arbitration Act, generally has been held to support the parties' choice of law to be applied in arbitrations, even in the face of explicit state law to the contrary, as discussed in question 39.

Unless the parties provide otherwise, the United Nations Convention on Contracts for the International Sales of Goods will govern contracts for sales of goods between parties who have their places of business in different contracting states, of which the US is one.

38 Are there restrictions on the parties' contractual choice of courts or arbitration tribunals, whether within or outside your jurisdiction, to resolve contractual disputes?

The parties can provide in the distribution contract for all litigation to be brought in a court located in a particular state or country and can waive their right to seek a transfer. These clauses are sometimes enforced and sometimes not. The Supreme Court, in *Burger King Corp v Rudzewicz*, has held that a franchisor can constitutionally enforce a forum-selection clause against its franchisees in an action commenced by the franchisor in its home state. Courts in the distributor's home state, however, may refuse to enforce a forum-selection clause on the ground that the public policy interests of the distributor's state outweigh the parties' choice. Note also that state franchise laws may expressly prohibit the choice of another state as a forum. Federal courts, however, will apply federal law to determine whether to enforce such a clause, notwithstanding any such state view; the forum clause is not dispositive, but should be considered together with the other factors normally weighed in a transfer motion, at least where the choice is between two federal districts.

A showing of state policy sufficient to outweigh a forum clause may be difficult to make. For example, Maryland courts have held that a forum selection clause favouring the franchisor's home state was enforceable despite being incorporated into a form contract where the franchisor had superior bargaining power, reasoning that there was no fraud involved, and a federal district court in New York upheld a one-sided forum clause that restricted venue in actions by a franchisee, but not in actions by the franchisor. In contrast, the District of Puerto Rico declined to transfer a dispute to California courts as required by a contractual forum clause, as Puerto Rico was more convenient for witnesses, and there was no evidence justifying transfer other than the contract clause.

As discussed in more detail in question 39, arbitration clauses specifying a particular forum are likely to be enforced under the Federal Arbitration Act. The Seventh Circuit US Court of Appeals reversed a district court decision and ordered arbitration in Poland pursuant to contract in a case under the Illinois Beer Industry Fair Dealing Act, holding that while the state's public policy expressed in that statute required Illinois law to apply notwithstanding the contract's choice of Polish law, that public policy could not overcome the Federal Arbitration Act policy in favour of arbitration.

39 What courts, procedures and remedies are available to suppliers and distribution partners to resolve disputes? Are foreign businesses restricted in their ability to make use of these courts and procedures? Can they expect fair treatment? To what extent can a litigant require disclosure of documents or testimony from an adverse party? What are the advantages and disadvantages to a foreign business of resolving disputes in your country's courts?

Suppliers and their distribution partners have access to both state and federal courts to resolve their disputes, although, as noted in question 4, a company that fails to file its qualification to do business in a state in which it meets the definition of 'doing business' usually will not be entitled to maintain any action or proceeding in the courts of the state. This rule applies to both US companies formed in other states and non-US companies, and in general foreign businesses have equal access to the courts. By and large, foreign companies can expect fair treatment in US courts, especially in the federal courts and courts of the larger commercial states. Some states, such as New York, have a well-established body of commercial law and have created specialised commercial courts with judges experienced in commercial disputes, making these courts a desirable forum for dispute resolution.

Discovery in US courts is very broad, typically requiring disclosure of documents and electronic materials, responses to written interrogatories and deposition testimony of witnesses whenever material and necessary in the prosecution or defence of an action. This does substantially increase the cost of litigation in US courts. In response, subject to showing a need for greater discovery, some courts have enacted rules that place limits on the length of depositions, the number of witnesses that may be deposed and the number of interrogatories that may be propounded. Electronic discovery of documents and email is also generally quite broad and can be a significant cost, although some courts may shift that cost to the party seeking the discovery in certain circumstances. In addition, federal and state courts have implemented rules to permit parties to seek to limit discovery so that it is proportionate to the value of the material sought and the value of the case.

Alternative dispute resolution methods may be agreed to by the parties, such as non-binding mediation or binding arbitration, discussed in response to question 40, and certain industry regulations and industry self-regulatory codes may provide or require certain disputes, such as a claim of wrongful termination, to be resolved before government agencies or industry boards.

40 Will an agreement to mediate or arbitrate disputes be enforced in your jurisdiction? Are there any limitations on the terms of an agreement to arbitrate? What are the advantages and disadvantages for a foreign business of resolving disputes by arbitration in a dispute with a business partner in your country?

A provision for binding arbitration of disputes in place of the courts will generally be enforced under the Federal Arbitration Act (FAA), which



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favours arbitration agreements, even in the face of state law to the contrary. Note, however, that where state law requires – as some state business franchise laws do – a disclosure that a choice of law or choice of forum provision, including an arbitration clause, may not be enforceable in that state, a question arises as to whether the parties really agreed to the provision. The Ninth Circuit US Court of Appeals has held that a contractual choice of forum for arbitration was unenforceable because of such a mandated disclaimer, finding that the franchisee had no reasonable expectation that it had agreed to arbitrate out-of-state.

Provisions limiting the relief arbitrators may award to actual compensatory damages, or expressly precluding punitive damages, injunctive relief or specific performance, will also generally be enforceable. The US Supreme Court has held that the FAA's central purpose is to ensure 'that private agreements to arbitrate are enforced according to their terms', so that the parties' decision as to whether arbitrators may award punitive damages will supersede contrary state law. Similarly, courts generally will also enforce a provision for a particular arbitration forum.

However, care should be taken in drafting arbitration clauses not to overreach, because even under the FAA, arbitration agreements may

be set aside on the same grounds as any other contract, such as fraud or unconscionability. For example, the Ninth Circuit held an arbitration clause unconscionable, and so unenforceable, where franchisees were required to arbitrate, but the franchisor could proceed in court. A district court in California rejected an arbitration clause as unconscionable where the arbitration clause blocked class adjudication (requiring each case to be resolved individually) and proved unfavourable for plaintiffs on a cost-benefit analysis. It is thus prudent to adopt a more balanced approach in drafting arbitration provisions.

Arbitration is private, in contrast to the courts and, depending on the court, can sometimes be faster and cheaper. It may afford less discovery and can present problems requiring testimony of non-parties, to the disadvantage of a party who needs them. There is generally no appeal from a legally incorrect or factually unfounded decision and arbitrators often seek a compromise result.

While there is no similar statutory underpinning for provisions requiring non-binding mediation before parties may proceed to court or binding arbitration, such a provision generally will be enforced under principles of freedom of contract.

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