

# Agency, Representation and Distribution Agreements in Asia

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## I. Foreign Laws Governing Rights and Duties of Commercial Agents, Distributors and Franchisees

### A. Japan.<sup>1</sup>

There is no uniform law dealing with distribution, consignment or agency agreements in Japan. Instead some aspects are provided for in the Civil Code or the Commercial Code.<sup>2</sup> The law of contracts governs the agreements, as does the law of sales and the law of agency (if there is an agency relationship). In addition the antimonopoly law, the security interest law, the law concerning debtor and creditor relationships and the tax law have significant impacts on such agreements in Japan. International agreements may be governed in part by laws concerning international trade, conflict of laws and foreign exchange. Courts also generally enforce contractual provisions which are not strictly covered by statutory provisions or even conflict with

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<sup>1</sup> See Kitagawa, Doing Business in Japan, Chapter 5, Agency and Distributorship, by Yoshinori Hosoya assisted by Anthony Zaloom.

<sup>2</sup> Japan is a civil law country, with much of the Civil Code originally modeled after the German Civil Code.

statutory provisions if they are not in violation of the good faith rule or public order.<sup>3</sup> In addition, in some cases, such as termination of a distributorship discussed infra, judge made law is very important.

**1. Distributorship.** Distributorships are the most frequently used method of sales representations in Japan. There is no strict legal definition of the term "distributor" or "distributorship". A distributor differs from an agent or consignee in that the distributor normally has the ownership right to, as well as possession of, the goods sold. However, for security purposes, in some cases the ownership right to the goods is retained by the supplier. Even here, the distributor is entitled to sell the goods as their own in the ordinary course of business. The relationship between the distributor and the supplier is a vendor-vendee. The distributor is not the agent of the supplier and has no fiduciary duties to the supplier in the absence of contractual provisions providing for such duties. Absent contractual provisions, the distributor is free to handle competing products and to sell goods to anyone chosen. Indeed in certain cases, a restriction on the free choice of customers may violate certain provisions of the antimonopoly law.

The distributor bears the risk of loss on credit sales and from unsold goods. All of the risk of damages to or loss of the goods after delivery is on the distributor, even if the ownership right to the goods is retained by the supplier as a security device. It is frequently provided by contract, but certainly not required, that the distributor has an exclusive territory and will not handle products of competing suppliers.

Japan does not have a uniform system of secured transactions similar to Article 9

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<sup>3</sup> Civil Code, Arts. 1, 90-92.

of the UCC. However there are certain security provisions which apply to sale of goods. The seller of personal property has a preferential right (*sakidori-tokken*), a security interest, created by statute without any documentation or registration, to secure payment for goods sold. However, in order to realize such security interest, the merchandise must be foreclosed in a rather cumbersome procedure. In some cases the proceeds are also subject to the preferential right. Priority is as provided in the Civil Code.<sup>4</sup>

There is also a title transfer security interest, judicially created, which has no statutory basis. Where such a security interest is created in a distributorship agreement, the goods sold to the distributor are reassigned back to the supplier when they are sold. If the goods are sold in the ordinary course, title passes to the purchaser. Against a third party, such as other obligees of the distributor, the supplier has ownership rights to the goods. This third party can not attach or execute on the goods to collect from the distributor. Upon default the supplier does not need to go through the statutory foreclosure procedure in order to realize on the security interest. A third security interest is to retain title by the seller until full payment is made. In this case, priority over other obligees of the distributor is even more clearly established. In some circumstances, the distributor is free to resell the goods in the ordinary course of business, with good title transferring to the purchaser of the goods. This is a creation of the contract between the supplier and the distributor and, like the title transfer security interest, provides for a faster realization on the security interest.

A continuing suretyship is widely used for Japanese distributorship relationships,

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<sup>4</sup> Civil code, Arts. 303-341

although mostly for domestic distributorships. The surety of a continuing suretyship guarantees the payment owed or to be owed by the distributor to the supplier. Ordinarily the amount guaranteed and the duration of the surety relationship are not fixed. This creates some problems which has led to a fair amount of litigation (for Japan) and judicially created limitations of the liability to that reasonably contemplated by the surety. It is also thought that a continuing suretyship could be terminated if there has been an unforeseeable and material changes in the circumstances which would seriously affect the liability of the surety.

Unilateral termination of a distributorship is not covered by any specific statutory provision in Japan. However, if the distributorship is not for a set period of time and if the distributor makes a substantial investment in reselling the supplier's products in anticipation that the agreement would continue for a long period of time, the parties are not free to arbitrarily terminate the agreement. Courts have laid down restrictions on arbitrary or immediate termination of agreements by the supplier without good cause. Termination for cause must be based on a breach so serious that it justifies the imposition of the termination of the distributorship on the distributor. Lost profits for a year is the damages which is most frequently awarded, although the circumstances of the breach severity, length of time of the distributorship, prior notice, amount of investment, or level of business obtained all have an impact on the amount of the damages.

It is not clear whether similar damages are available in cases of refusal to renew a distributorship of a fixed term. However, if the term is relatively short, has been consistently renewed in the past and the parties reasonably anticipated that it would be

renewed, the distributor termination would probably be subject to the same damages as termination of an indefinite period distributorship. However, a fixed term is advisable for the supplier if it is possible. Grounds for termination should be as concrete as possible, with standards for performance spelled out. The agreement may also spell out certain payments or compensation for termination for any reason as a way of avoiding the uncertainty of a damages claim.

**2. Agency.** The word agency (*dairi*) has a broad meaning and is rather a general term. Under the Civil and Commercial Codes, the term describes one empowered to act on behalf of the principal. The agent is not a party to a sales contract at all but rather if the agent executes a contract on behalf of the principal, the principal becomes the seller. An agent as a sales representative is an independent merchant who makes repeated sales of the goods of his principal. Ordinarily the sales agent does not have possession of the goods but only has samples. The agent is not an employee of the principal. The sales agent is authorized to execute a contract for the sale of goods of the principal, which contract is directly binding on the principal.<sup>5</sup> The principal may, by contract limit the authority of the sales agent to, for example, only certain goods or certain territory. In certain cases, the act of an agent outside the authority of the agent, may still be binding on the principal under "apparent agency" (*hyoken-dairi*), when the principal by its acts leads a third party to believe that the agent is within the agent's authority.

The agent has a fiduciary responsibility to the principal. Thus the agent can not act for a competitor without the permission of the principal. Unless otherwise agreed in

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<sup>5</sup>Commercial Code, Art. 46.