

[Introductory Note. This is a checklist for drafting distribution agreements (agreements in which one party – typically a manufacturer – contacts with another party – the distributor – to arrange for the sale in commerce of the manufacturer's product(s)).

For any business, particularly a small business, a distribution agreement can be among the most important contracts the business enters into.

Non-lawyers can use this checklist to prepare for meetings with lawyers engaged to prepare distribution agreements. Having answers to – or at least considering – all of these issues will reduce the amount of time spent consulting with the lawyers. This should reduce cost significantly.

Lawyers can use this checklist to prepare for meetings with clients, and to make sure they have addressed all of the major issues in the definitive agreement.

As with all of my documents, nothing in this document is intended as legal advice in any jurisdiction, and I express no opinion on the substantive law of any jurisdiction. While the principles of law affecting distribution agreements is reasonably consistent in most U.S. jurisdictions, there are some differences between generally prevailing domestic law and the laws in other countries.

Additionally, applicable law on distribution agreements is highly fact-specific, particularly if either the manufacturer or the distributor is a large enterprise or has “market power” in the product(s) to be distributed. Also, there may be significant financial effects on companies that are issuers of publicly traded securities of some of these provisions (e.g. return of product, etc.). Such issuers should consult their financial staff and their auditors.

Non-lawyers are urged to engage competent counsel for preparation of any distribution agreement. This is particularly true if the agreement is to operate outside the U.S. or if either party has “market power” in the product(s) to be distributed.

Finally, these questions are not intended to suggest specific answers. Asking “Will there be ...?” does not mean there should be. Often, the opposite is true.]

Basic Checklist for Drafting Distribution Agreements

1. The Parties

- (a) Identify each by proper company name, address, and state of corporation.
- (b) If a partnership, include the name of the partners and the name of the partnership.

- (c) If a sole proprietorship, include the name of the business and the name of the proprietor.
- (d) Bottom line: Are each of the parties creditworthy such that a suit to enforce the agreement is worth contemplating?
- (e) Identify the relationship of the parties. (You may want to include a provision denying that parties are partners, joint venturers, agents, etc.)

2. The Products

- (a) Is the agreement to cover all of the products made by the manufacturer or some subset of those products?
- (b) Is the agreement to cover any/all of the products introduced by the manufacturer in the future?

3. Trademarks and Trade Names

- (a) Which, if any, trademarks and trade names does the agreement cover?
- (b) Does the agreement cover trademarks or trade names that the manufacturer may obtain in the future?
- (c) What rights in the trademarks and trade names will the distributor have?
- (d) Is the distributor's use of trademarks and trade names to be limited to advertising?
- (e) May the distributor use as part of its business name the manufacturer's trademarks or trade names, or will that be specifically prohibited?
- (f) Must the distributor follow the manufacturer's trademark and trade name guide?
- (g) Must the distributor obtain the manufacturer's approval for every use of the manufacturer's trademarks and trade names?

4. Territory/Customers

- (a) Is the distributor's territory exclusive?
- (b) Is there a designated primary area of responsibility?
- (c) May the manufacturer make direct sales, for example, by mail order? Internet?

- (d) What about sales to the U.S. government?
- (e) Are there any "reserved" accounts, such as "national accounts" or established accounts directly between the customers and the manufacturer?
- (f) Is there to be a specific location clause?
- (g) Can locations be added within the territory in the future?
 - i. If so, are there any stated criteria the distributor must meet in order to obtain new locations?
- (h) What about drop shipments to customers' facilities?
- (i) Is the manufacturer to forward to the distributor any inquiries received from the customers in the distributor's territory?
- (j) What happens if the distributor sells outside of its territory?
 - i. Is there to be a "profit passover"?
 - ii. Will the distributor be required to issue reports?
 - iii. Is any approval required?
- (k) Will a distinction be made between products the customer picks up at the distributor's location with the bill sent outside the territory and products shipped directly outside the territory?

5. Other Distributors/Sales in Distributor's Territory

- (a) What happens if other distributors of the manufacturer sell in this distributor's territory?
- (b) Will the distributor be entitled to compensation (i.e., to receive a profit passover)?
- (c) Will the manufacturer also be acting in a distributor capacity in this distributor's territory, thereby giving rise to a dual distribution situation?

6. Competitors' Products

- (a) May the distributor handle competitors' products?

- (b) If the distributor may handle competitors' products, are there any restrictions, such as giving the manufacturer's product "most-favored" treatment or limiting competitive products to a certain percentage of the distributor's total inventory of a given type of product?

7. Full Line

- (a) Is the distributor required to handle a "full," "representative" line?
 - i. If so, is that adequately described?

8. Term and Termination

(WARNING: CRITICAL – TERMINATING DISTRIBUTORS ALMOST INEVITABLY RESULTS IN LITIGATION.)

- (a) Is the agreement to be for a fixed term?
- (b) Is the agreement to be for a fixed term plus renewal:
 - i. automatically without notice; or,
 - ii. automatically with notice (in other words, if the manufacturer gives notice that the agreement is to terminate on the specified date, it does so; but, if the manufacturer does not provide advance notice of automatic termination, the agreement does not terminate)?
- (c) Will there be an “evergreen” provision (automatic renewal)?
 - i. If so, what is renewal term?
 - A. Initial term (which may be for many years so the distributor has an incentive to invest in the business of distributing the product)?
 - B. Lesser term?
- (d) May the distributor be terminated for any of the following reasons:
 - i. the distributor's financial situation;
 - ii. the distributor's failure to pay bills;

- iii. the distributor's failure to meet quotas;
 - iv. the distributor's failure to uphold all the terms of the agreement;
 - v. the distributor's failure to maintain the required inventory;
 - vi. the distributor's conviction or settlement of any criminal, regulatory or civil offenses (environmental, occupational health and safety, consumer protection/fair trade, etc.) adversely reflecting on the manufacturer;
 - vii. the distributor sues the manufacturer;
 - viii. the distributor becomes a competitor of the manufacturer;
 - ix. acts of the distributor adversely affecting the goodwill of the manufacturer or the product;
 - x. the distributor's submission of false or fraudulent reports, forms, or certifications; a change in control or management of the distributor; any dispute, disagreement, or controversy between or among principals, partners, managers, officers, or shareholders of the distributor which, in the opinion of the manufacturer, may adversely affect the business; or
 - xi. a change in marketing strategy?
- (e) May either party terminate the agreement without cause?
- i. If so, what period of notice or opportunity to cure, if any, is required?
- (f) Does the termination notice have to state the reason for the termination or nonrenewal?
- (g) Will the manufacturer, upon termination, have the right or the obligation to repurchase all or a portion of the unsold stock upon proper notification?
- (h) Upon termination, will the distributor have to remove the manufacturer's marks or insignia?
- i. If so, how will price be determined?
- (i) Is the right to terminate the distributor limited by state industry laws, state franchise laws, or special industry statutes that might apply?

- (j) Are there any statutory limitations on the right to terminate for good cause?
- (k) Are there any rights the manufacturer will want to assert after the termination, such as a noncompete clause?
- (l) Which provisions of the agreement survive termination?

9. **Minimum Purchases**

- (a) Are there minimum purchases for individual orders?
- (b) Are there monthly, annual, or other quantity requirements?

10. **Inventory**

- (a) Must the distributor maintain a minimum quantity of inventory?
 - i. If so, is it inventory of the manufacturer's products in general or inventory of specific products?
- (b) Will there be any "stock lifting"?

11. **Distributor's Facilities**

- (a) Are there any requirements for the distributor's facilities, such as storage requirements, stock rotation requirements, and the like?
- (b) Is there a minimum square footage requirement?
- (c) Is there a requirement for the number of employees?
- (d) Must the distributor display a sign?

12. **The Distributor's Customers**

- (a) May the distributor sell to other dealers or other distributors, or only to end users?
- (b) Are there to be different prices or discounts depending upon the level of distribution or redistribution?
- (c) If there are different price levels, is there a system for keeping track of the sales made to the different levels of distribution?

13. **Prices**

- (a) How are the prices charged to the distributor to be calculated (e.g., a percentage off the list price or a stated price)?
- (b) Are the prices to be established at the time the distributor places the order or when the goods are delivered?
- (c) Is there to be protection against price increases for orders in process?
- (d) Is there to be notice of some price increases so that the distributor can order under the existing prices?
- (e) Does the agreement give the manufacturer has the flexibility to change its prices at will (or with certain advance notice)?
- (f) Should the agreement state that the distributor is free to set its own prices?

14. **Terms of Sale**

- (a) Are the terms of sales to the distributor to be included in the distributorship agreement?
- (b) Is there a provision stating that no purchase order or sales forms will be applicable, but instead the terms and conditions in the distributorship agreement will govern, in order to avoid a battle of the forms?

15. **Warranties**

- (a) Does the manufacturer warrant the goods to the distributor or the end user?
- (b) What rights or obligations does the distributor have with respect to the manufacturer's warranties:when it sells:
 - i. to other distributors; or
 - ii. to end users?

16. **Promotional Allowances**

- (a) If the manufacturer offers promotional allowances, is the distributor's participation optional or mandatory?

- (b) Can the distributor require the manufacturer to offer promotional allowances or advertising sharing programs?
- (c) Are set amounts or percentages of sales required for either the distributor or the manufacturer?

17. **The Distributor's Finances**

- (a) Must the distributor make its financial data available to the manufacturer?
- (b) Is the manufacturer allowed to audit that information?
- (c) Must the distributor maintain a stated amount of capital or may it meet a more generalized standard of "adequate capitalization"?
- (d) Will the manufacturer have a right to terminate the distributorship for insolvency?
- (e) Will the manufacturer have the right to terminate for some lesser financial problem, and if so, is that stated clearly and specifically?

18. **Employee Raiding**

- (a) Can the distributor solicit the manufacturer's employees?
- (b) Can the manufacturer solicit the distributor's employees?
- (c) If the parties cannot solicit the employees of the other?
 - i. Can they hire employees who solicit employment independently?
 - ii. Can they hire former employees?
 - A. If so, is there a minimum time limit (e.g. after the employee has no longer been employed by the other party for 1 year, etc.)
- (d) How will confidential information of a former employee of the other party be protected?

19. **Technical Qualifications**

- (a) What training must the manufacturer offer?

- (b) What training may the manufacturer offer?
- (c) What training is optional for the distributor?
- (d) What training is mandatory for the distributor?

20. **Warranty and Maintenance Work**

- (a) Will the distributor be authorized or required to provide warranty service or maintenance of products?
- (b) What will be the required technical qualifications of the distributor's service employees?
- (c) What training will the manufacturer provide for the distributor's service employees?
- (d) What parts will the manufacturer provide to the distributor?
- (e) How is payment for the warranty services to be structured?

21. **Hazardous Chemicals**

- (a) Must the manufacturer notify the distributor of any hazardous chemicals contained in the product?
- (b) What responsibilities, if any, does the distributor have for product stewardship?

22. **Defects or Damage and Indemnity Claims**

- (a) Must the distributor notify the manufacturer of any claims that it receives of defect or damages concerning the goods?
- (b) Will manufacturer defend and indemnify distributor for all product liability claims?
- (c) Will manufacturer defend and indemnify distributor only for bodily injury product liability claims for which manufacturer is potentially liable on a strict liability theory?
- (d) Will the distributor indemnify manufacturer for warranties made by the distributor (such as fitness for purpose) or for distributor's negligence?

23. **Support**

- (a) Must the manufacturer provide ongoing technical support to the distributor?

- (b) Must the manufacturer provide service representatives?

24. **Payment Terms**

- (a) Will the payment terms be net thirty days or something else?
- (b) Will the manufacturer offer prompt payment discounts?
- (c) Will the manufacturer charge late payment penalties or interest?

25. **Distributor's Right to Return Products**

- (a) Will there be any limits on the dollar amounts of products the distributor may return?
- (b) Must the returned products be in "resalable condition"?
- (c) Must the returned products be in their original cartons or packaging?
- (d) Will the manufacturer give a refund or a credit?
- (e) Will there be any specific time limits for return (e.g., the distributor cannot return a product after one year)?

26. **Purchase Estimates**

- (a) Must the distributor provide estimates of the amount of product that it plans to purchase?

27. **Delivery**

- (a) Does the agreement state delivery terms (such as F.O.B. point)?
 - i. Note: "F.O.B." was used in this outline because it is commonly recognized. It is not commonly understood. F.O.B. – whether under the Uniform Commercial Code or Incoterms – only applies to transportation by ship. Unless you are dealing in a product delivered by "vessel" (ship), do not use F.O.B. And, use Incoterms exclusively.
- (b) Does the agreement state who will pay the freight charges, if not clear from the delivery terms?
- (c) Does the agreement designate a carrier or specify which party designates the carrier (if

- not clear from the delivery terms)?
- (d) Does the agreement state who will be responsible if the carrier loses or damages the goods (When does risk of loss transfer)?
 - (e) Does the agreement specify who is responsible for procuring and paying for insurance on the goods during transportation (if not clear from the delivery terms)?
 - (f) If not clear from the delivery terms, does the agreement specify when title to the goods passes from the manufacturer to the distributor?
28. **Billing**
- (a) Will the manufacturer bill the distributor or is the distributor expected to pay from the shipping documents?
 - (b) If there is to be a discount, is it to be measured from the date the manufacturer sends the bill or from the date of shipment?
29. **Inspection, Testing, Counting**
- (a) What right does the distributor have to test, inspect, and count the goods?
 - (b) Will there be a time limit on the exercise of these rights (e.g., thirty days from delivery, presumed acceptance after that)?
30. **Notice**
- (a) Must the manufacturer give the distributor advance notice of new products?
 - (b) Must the manufacturer give the distributor advance notice of changed specifications?
31. **Continuous Availability**
- (a) Will the manufacturer provide a continuous availability of spare parts, products, service, and/or product documentation?
 - (b) Does the manufacturer have the right to allocate deliveries among all of its customers on a reasonable basis if the manufacturer experiences a shortage of products?
32. **Instruction Manuals, Technical Data**
33. What requirements should be stated for instruction manuals, technical data, etc.?

34. **Infringement Actions**

- (a) Will the manufacturer hold the distributor harmless from patent, copyright, trademark, or other infringement actions?

35. **Confidential Information**

- (a) Will the manufacturer be required to hold the distributor's information in confidence?
- (b) Will the distributor be required to hold the manufacturer's information in confidence?
- (c) Will confidentiality agreements be mutual?

36. **Orders**

- (a) Are orders subject to the manufacturer's acceptance?
 - i. If so, at what location?

37. **Insurance**

- (a) Will either party require the other to obtain any type of insurance policies, such as commercial general liability, workers' compensation, product liability, and the like?
- (b) Will a party requiring insurance be named "additional named insured" on the policy?
- (c) Will a party requiring insurance receive a certificate of insurance? Will the certificate provide 60 days prior notice of cancellation?

38. **Miscellaneous**

- (a) Does the agreement contain provisions covering the following terms and conditions:
 - (b)
 - i. force majeure,
 - ii. taxes,
 - iii. assignment,
 - iv. records/audits,access to facilities,
 - v. nonwaiver,

- vi. severability,
 - vii. section headings,
 - viii. choice of law,
 - ix. choice of forum,
 - x. entire agreement, no oral modifications,
 - xi. alternative dispute resolution/arbitration,
 - xii. notice (i.e., in writing, where to send, etc.),
 - xiii. international distribution issues, and
 - xiv. definitions of terms?
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