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## Local Distributor Partnerships: Investigate Before You Terminate

Foreign companies usually opt to appoint their local distributors as the local entity to apply for and maintain product registration and import licenses, as usually required by Asian FDAs and Ministries of Agriculture. Such appointments are normally set out in the distribution agreement. While on most occasions this is a mutually beneficial relationship, sometimes local partners who have built up the business for those products may begin to compete unfairly or commit other breaches that lead to difficulties in terms of terminating a partner.

### Determination of Acceptable Breach

All commercial relationships have their ups and downs, which may not reach a level of acceptable breach to warrant a termination. Economic turndowns, weather conditions, increased competition, and other situations are all reasonable events whereby you and your local partner may need to reposition and revisit minimum sales targets and advertising spend. However, as soon as relations appear unstable and reports of unsatisfactory performance start coming in regularly, the foreign partner should look closely into the conduct of its local partner in order to head off what may amount to warranted termination.

Simple searching will reveal that your partner is disregarding your agreement. The distribution agreement likely has a clause allowing you to visit, unannounced, to inspect. In other circumstances, checks like this can also be made at the relevant Companies Registry, Ministry of Commerce, tax office, etc.

Frequently observed examples of breaches are:

- ◇ Registration of a similar trademark for an identical product
- ◇ Manufacture and/or sale of a competitive product without authorization
- ◇ Non-observance of the target without any reasons or notification given
- ◇ Conspicuous decrease in sales of some products while maintaining adequate sales of others

### Agreement Review

Your next step is to go through the terms of your agreement with the partner carefully to determine whether these infringements may amount to a material breach, and to pinpoint the consequences for such breaches or infringements.

Another important step is to clearly check the dispute resolution and termination process in the agreement. You may find that arbitration is the stated dispute resolution procedure or that there has been a carve out for court injunctive relief on the occurrence of IP infringement. In the latter case, you can go to court immediately to seek an injunction.

You must check whether termination is effective immediately or after a prescribed period of time. If there is a breach, the termination process should be clearly followed, as the local partner may deny any wrongdoing on his or her part. Here, your paper trail of earlier warnings will be very helpful.

### Notification Before the Termination

The termination notice should:

- ◇ Include a list of all breaches in order to reduce the chance of the distributor thinking he or she can challenge the allegations
- ◇ Be carefully worded
- ◇ List all documents to be returned for a clear termination of the relationship, including the Certificate of Free Sale and cancellation of the Import License, in order to discourage your local partner from pursuing further unauthorized sales

When the situation with a breaching distributor has passed the point of no return, you have to check the name under which products were registered. In Thailand, products are required to be registered in the name of a local entity.

An amendment of the application is not possible and the foreign company has to reapply to obtain a new product registration certificate. The advantage of this method is that the local partner may not be aware of such new applications. The inconvenience is that it may take a few months before the new Product Certificate is granted, costs will be incurred, and sometimes retesting is required.

It is in the interest of the foreign company to finalize the complete process and change to a new distributor as soon as the termination is effective. However, you should first check whether an application for the same product is contrary to the terms of your agreement, especially in regard to anticompetition rules or exclusivity granted to the distributor. 🐼

### Compliance Audit

A Compliance Audit is normally advised either during the course of or immediately after regulatory complaints. Compliance Audits are conducted by a team of lawyers and/or paralegals visiting local offices in order to review, collect, and assess those areas of the business that are susceptible to additional regulatory scrutiny. Typically, a Compliance Audit would encompass review of:

1. Advertising and promotional materials (past, current, and planned)
2. Product labels, product inserts, and product packaging (past, current, and planned)
3. Thai FDA product registration certificates
4. Customer complaint procedures
5. Organizational structure
6. Other areas as observed during the course of the Compliance Audit

A Compliance Audit is usually conducted in about one day. Findings are assessed in order to prepare the Compliance Audit Report. The Compliance Audit Report aims to assist with effecting policies and procedures to confirm continual compliance with evolving legislation and regulations. This Report sets out the practical advice and suggested strategies to identify how current processes, policies, procedures, legal agreements, and practice could be supplemented to minimize and manage the types of risks the business is currently dealing with. The investment required to conduct a full-day assessment visit and develop the follow-up Compliance Audit Report depends on several factors including (1) the level of cooperation with your local company, (2) the amount of documentation requiring assessment as discovered during the assessment visit, and (3) the scope of the review in terms of how many years of business we think necessary to include in our assessment. By knowing what risks remain and by formulating and implementing effective procedures and policies to end these, business vulnerability can be decreased significantly.