

China Distributor Agreements: Protecting Your Brand and Payment

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Unofficial English translation prepared for reference only. The official Chinese text prevails.

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A distributor in China isn't just a sales channel. For a foreign company without a local entity, the distributor is the face of the brand, the owner of the customer relationship, and the gatekeeper to market intelligence. A distributor that underperforms can damage a brand more effectively than a competitor — because the competitor has to overcome customer inertia, while the distributor has direct access to the customers.

The distributor agreement is the foreign company's primary tool for managing this relationship. A well-drafted agreement doesn't guarantee a good outcome, but a poorly drafted one practically guarantees problems.

Exclusive vs Non-Exclusive

The first structural decision is exclusivity. An exclusive distributor has the sole right to sell the foreign company's products in a defined territory — typically all of China or a specific region. In return for exclusivity, the distributor usually commits to minimum purchase volumes and annual growth targets.

Exclusivity creates an alignment of incentives that a non-exclusive arrangement doesn't. The exclusive distributor has an incentive to invest in building the brand because it captures the returns from its investment. A non-exclusive distributor that builds up a brand knows that another distributor can ride on its efforts and undercut it on price.

The risk of exclusivity is that the distributor doesn't perform. The foreign company is locked in — it can't appoint another distributor in the same territory without terminating the exclusive distributor, which may trigger contractual damages or litigation. The exclusivity clause must therefore be paired with performance requirements that give the foreign company the right to terminate or convert to non-exclusive if the distributor doesn't meet its targets.

Territory and Channel Restrictions

The territory definition should be precise. "China" as a territory for an exclusive distributor is a big commitment covering a market of 1.4 billion people across thirty-one provinces with dramatically different economic conditions. A more common structure is provincial or regional exclusivity — Guangdong Province, the Greater Bay Area, East China — with the foreign company retaining the right to appoint distributors in

other regions or to sell directly to certain customers.

Channel restrictions are equally important. The distributor agreement should specify whether the distributor can sell online, and if so, through what platforms and on what terms. An distributor that's authorized for offline distribution in Guangdong but starts selling on Pinduoduo at prices that undercut the foreign company's other channels is a problem that could have been prevented with a clear channel restriction.

The agreement should also address sub-distribution. If the distributor can appoint sub-distributors, the foreign company should have approval rights over the sub-distributors and the right to receive information about their sales and activities. A sub-distribution network that the foreign company doesn't know about and can't control is a risk to brand positioning and pricing integrity.

Pricing and Payment Terms

The pricing provisions need to balance the foreign company's interest in maintaining brand positioning with the distributor's need for commercial flexibility. A minimum resale price prevents the distributor from discounting the brand to compete on price, but maximum resale prices can raise competition law issues in some markets.

The more practical concern for most foreign companies is payment. A distributor that takes goods on credit and then pays late, or doesn't pay, is a universal problem. The payment terms should be specific and enforceable. A letter of credit from a Chinese bank provides the strongest payment security. A deposit or advance payment, or payment against documents, reduces exposure. Open account terms — goods shipped and paid for within thirty, sixty, or ninety days — should be limited to distributors with an established payment history and should be secured by a parent company guarantee or a standby letter of credit.

The agreement should include interest on late payments at a rate that's commercially meaningful and enforceable in China. A rate of 0.05% per day on overdue amounts — roughly 18% per year — is common in Chinese commercial practice and supported by Chinese law.

Brand Protection and IP

The distributor agreement is an IP protection tool as much as a commercial contract. The distributor should acknowledge that the foreign company owns all IP in the products, the brand, and the marketing materials. The distributor's right to use the brand is limited to the distribution of the products and terminates when the agreement ends.

The agreement should prohibit the distributor from registering the foreign company's trademarks, domain names, or company names in China. This provision, backed by a contractual penalty, is a deterrent against trademark squatting by a distributor — a depressingly common problem.

The distributor should be required to promptly notify the foreign company of any infringement of the foreign company's IP that it becomes aware of, and to cooperate in enforcement actions. A distributor that discovers counterfeit products in its territory has an obligation to report them and to assist in the enforcement process.

Termination and Transition

The termination provisions are the most important part of the agreement because they're what the foreign company relies on when the relationship isn't working. The agreement should include termination for convenience with a notice period — typically three to six months for a significant distribution relationship. Termination for cause should cover material breach, failure to meet minimum purchase obligations, insolvency, change of control, and damage to the brand.

The transition provisions matter because terminating a distributor without a plan for what happens next creates a gap in the market. The agreement should require the distributor to cooperate in the transition —

introducing the foreign company to key customers, transferring customer records, returning unsold inventory, and ceasing use of the brand within a specified period.

Chinese law provides statutory protections for distributors in certain circumstances, including compensation for the loss of the distribution right if the distributor has made significant investments in developing the market. These provisions derive from the protection of commercial agents under the Civil Code and can apply to distributors as well as agents. The agreement should address these statutory rights and, where possible, agree on the compensation mechanism in advance.

Dispute Resolution

The dispute resolution clause in a distributor agreement between a foreign company and a Chinese distributor requires more thought than a standard arbitration clause. Arbitration in China — typically at CIETAC, the China International Economic and Trade Arbitration Commission, or at the HKIAC in Hong Kong — is the standard recommendation for cross-border disputes. CIETAC awards are enforceable in China under the Arbitration Law, and in most other countries under the New York Convention.

The governing law choice creates a trade-off. Chinese law is favorable to distributors in some respects — the statutory protections mentioned above — but is more likely to enforce contractual penalty provisions and liquidated damages clauses than common law courts. The law of the foreign company's home jurisdiction may be more familiar but creates enforcement challenges if the distributor's assets are in China.

The practical recommendation is usually CIETAC arbitration in China with Chinese governing law, or HKIAC arbitration in Hong Kong with Hong Kong law and an express waiver of the distributor's statutory protections to the extent permitted by law. The choice depends on the bargaining power and risk tolerance of the parties, but the enforceability of the award against assets in China should be the primary consideration.