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Contracts Corner: Distribution Agreements

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Finding the right distributor is critical to the success of an alcohol brand—as is ensuring the agreement appointing that distributor provides ample protection for the supplier or brand owner. At a high level, suppliers should keep the following top of mind when entering into a distribution relationship or negotiating a distribution agreement:

(1) What **territory** do you wish the distributor to service? Consider the following: Does the distributor call on the accounts/channels that a supplier wishes to target with its brand? Does the distributor have the capability, sales force and reach to cover the entirety of the area assigned, whether it be a portion of a state, a region or the entire country? Where not mandated by franchise law, does assigning exclusive distribution territories make sense, or is dualing the brand a better option?

(2) Whether a state has **franchise law** applicable to the distribution of its product that will govern the relationship between supplier and wholesaler. With respect to the term and termination provisions of a contract, whether the state(s) where the distributor will handle products have franchise laws may heavily impact what within a distribution agreement is ultimately enforceable. This is particularly important in states that have alcohol franchise protections that make the termination of a wholesaler difficult. Distilled spirits and wine manufacturers should take advantage of the fact that far fewer states have franchise protections for the distribution of spirits than those that have franchise laws applicable to the distribution of malt beverages.

(3) What **sales goals** or distribution targets do you want the distributor to achieve? You can bake sales goals into a distribution agreement or agree to affix sales goals in annual planning or marketing meetings.

(4) What allocations will be made for **marketing**, if any? Contemplate the use of a marketing fund in a distribution agreement. These funds are often funded by both parties, with the use of the funds mutually determined by the parties during annual planning meetings. Note that a limited number of states prohibit these funds, or they require participation in them on the part of a wholesaler to be voluntary as opposed to compulsory.

(5) What factors will determine whether the distributor is adequately **servicing a brand**? Carefully

spelling out what the obligations and expectations of a distributor are is critical to creating a successful distribution relationship. Include measurable and specific obligations, particularly in states where good cause must be established in order to terminate a relationship.

(6) What events trigger the **termination** of the distribution agreement or relationship? Consider both events that may trigger a for-cause termination and not-for-cause termination rights (typically after payment of a termination fee).

(7) How to address a **change in control** of the parties. Change in control terms in a contract should address a change in control within a wholesaler's *and* a supplier's business. Suppliers should advocate for approval rights and the right to request reasonable information about a new owner or another fundamental change of a wholesaler, even in franchise states. For changes in control within a supplier's business, advocating for ample flexibility is critical, particularly for a brand that may one day wish to be sold.

(8) Address **supply constraints**, especially for small brands. The supply chain crisis continues to create volatility across almost all industries, and the alcohol industry has not been immune. For example, if negotiating a new distribution agreement, ensure that a supplier's inability to secure capacity from a contract manufacturer, if utilized, does not constitute a breach.

(9) Discuss the potential of **market withdrawal**. Market withdrawal and re-entry are possible, particularly for a brand that is growing and exploring its success in new markets. Advocate for the ability to withdraw and re-enter the market with a distributor that makes the most sense at the time of re-entry. Note that in states that have alcohol franchise protections, there is sometimes a period for re-entry that would require the brand to go to the previously assigned wholesaler.

(10) Determine the intention with respect to **new brands** and **brand extensions, especially across categories**. Consider whether you automatically want to assign any new brand or brand extension you produce, including those that cross category, to the wholesaler appointed for an existing brand in a territory and whether or not that brand should be added to an existing agreement or assigned via a new category-specific agreement.

(11) What happens after the **relationship ends**? Include terms in your distribution agreement that address the winding down of the relationship.

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