

SWISS INVESTMENT REPORT* 11

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The Swiss Investment Report is especially designed for Chinese Investors, who are intending to extend their business to Switzerland or Europe or are already doing business in Switzerland.

Of course, the Swiss Investment Report is also addressed to any other person who is interested in obtaining background information on the Swiss investment-related legal framework as well as information on current developments in the Swiss legislation from a foreign investor's perspective.

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Distribution

I. Introduction

Besides its excellent infrastructure, Switzerland provides a flexible legal framework for foreign companies to establish efficient distribution systems if they intend to sell their products in Switzerland and the greater European area. The most important channels for foreign suppliers to sell their products in Switzerland are local agents and distributors (*indirect distribution*). Depending on the circumstances, a foreign company may also consider distributing its products or services through its own affiliates, such as local branches and subsidiaries or through employed sales persons (*direct distribution*). If a supplier or manufacturer wants to keep full or major control over the distribution, he usually chooses to setup a direct distribution system. In case the distributor shall be more independent regarding his activities or shall even bear the distribution risk, the manufacturer should mandate an agent or distributor respectively. Different distribution channels are subject to different legal frameworks and this report shall give an overview over the contractual distribution systems provided by Swiss law.¹

II. Agency Agreement (Art. 418a et seq. CO)

According to the Swiss Code of Obligations (“CO”), an agent is a person who is mandated, on a continuous basis, either to act as an intermediary for transactions on behalf of the principal (“*Vermittlungsagent*”), or to conclude such transactions in the name and on account of the principal (“*Abschlussagent*”). Even though an agent is not employed by the supplier and can therefore freely organize his activities, he is rather dependent on the principal compared to a commission agent or a broker. The agent’s remuneration is commission based. If not agreed otherwise, the commission becomes due as soon as a valid contract has been concluded as a result of the agent’s activity.

¹ For more information regarding the establishment of subsidiaries in Switzerland, see Swiss Investment Report No. 3.

Even though agency agreements are not subject to any formal requirements, written contracts are recommended. Generally, the parties to an agency agreement can freely negotiate its content. However, in order to protect the agent's interests, statutory law provides several restrictions which must be kept in mind.

A. Delcredere liability

If not agreed otherwise, the agent is not liable for the performance of the contract with the single customers, i.e. for the fulfillment of the customer's obligations (*delcredere liability*). The agent shall bear such delcredere risk only if this is agreed in writing and in return, the agent will have an inalienable right to an appropriate special compensation.

B. Inalienable goodwill payment

Swiss law further provides an inalienable right to compensation for clientele after termination of the agency agreement (*goodwill payment*) if the following conditions are met: (i) The agent has substantially increased the principal's clientele through his activity; (ii) the principal substantially benefits from the business relations established by the agent, even after the termination of the agency agreement; and (iii) the termination of the agreement was not caused by the agent. The goodwill payment shall not exceed the average amount of net earnings derived from the agency relationship within one year.

C. Restrictions on non-competition clauses

The Swiss CO does not provide for any exclusivity rights and therefore, if not agreed otherwise, the principal and the agent may compete with each other during the agency relationship and afterwards. In case the parties agree on a non-competition clause, such clause is subject to the same restrictions as a post-contractual non-competition clause for employees. First, the non-competition clause must be agreed in writing. Second, it must be limited in terms of time (not more than three years), territory and scope of business. In contrast to an employee, the agent has an inalienable right to an adequate

compensation if the parties agree on a post-contractual non-competition clause.

III. Commission Agency (Art. 425 et seq. CO)

In a commission agency, the principal mandates the commission agent with the sale or purchase of movable goods or securities in the commission agent's name but on the account of the principal ("*indirekter Stellvertreter*") against payment of a commission. The commission becomes due as soon as the sales or purchase contract is executed. Even though the commission agent sells the commission goods in his own name, he becomes at no time the owner of these goods, if not agreed otherwise in the commission agreement. Therefore, the principal has a statutory right to take the commission goods back in case the commission agent goes bankrupt. Further, all payment claims of the commission agent deriving from the sales contract will automatically be assigned to the principal ("*Legalzession*") as soon as the latter has fulfilled all its obligations towards the commission agent.

The commission agency is widely-used within the scope of securities or art and antiques transactions. In contrast to the agency agreement, a commission agency is not necessarily based on a continuous relationship.

IV. Contract of Brokerage (Art. 412 et seq. CO)

According to the Swiss CO, a broker is mandated to act as an intermediary on behalf of the principal ("*Vermittlungsmakler*") or to supply information about potential business transactions ("*Nachweismakler*") against a commission. A broker does not conclude any contracts with third parties, be it in his own name or in the name of the principal, and acts on a case by case or single deal basis. The commission becomes due as soon as the broker's conciliation activity results in the conclusion of a contract between the principal and the third party.

Brokerage contracts are usually used for transactions such as real estate acquisition, tenancy agreements, employment contracts or investment and financing transactions.

V. Distribution Agreement

Despite its importance in practice, the distribution agreement is not statutorily regulated by Swiss law. A distribution agreement is therefore a mixed contract, i.e. a combination of several types of contracts defined in the CO. The distributor is usually entitled and obliged to buy the supplier's products in order to resell them in a particular territory. The distributor is furthermore obliged to promote the product in the allocated territory. The distributor works independently and on his or her own risk. Thus, the distributor's remuneration depends on the quantity and pricing of the resale transactions.

A distribution agreement can be established on an exclusive or non-exclusive basis. Unless agreed otherwise, exclusivity prohibits the supplier from mandating other distributors or directly distributing his products within the allocated territory.

According to established legal practice, some mandatory provisions regarding the agency agreement also apply to the distribution agreement as follows:

A. Inalienable goodwill payment

It had been disputed for many years whether a distributor shall be entitled to inalienable goodwill payment by analogy to the corresponding provision ruling the agency agreement. In 2008, the Federal Swiss Supreme Court finally decided on this question in favor of the distributor. According to this decision, a distributor shall be entitled to goodwill payment, if (i) the distribution agreement limits the distributor's autonomy in a way that his position is shifting closely to the one of an agent (e.g. minimum purchase and/or stock requirements, duty to disclose business records etc.) and (ii) the clientele of the distributor remains loyal to the supplier after termination of the distribution agreement. This is usually the case if the distributed products are well-known branded products. To be entitled to an inalienable goodwill payment, the prerequisites as stated for the agency agreement (see section II. B) must be fulfilled additionally.

B. Non-competition clause

The parties to a distribution agreement are free to agree upon non-competition during the term of the distribution agreement and/or for the time after its termination. However, post-contractual non-competition clauses may not exceed a one-year term pursuant to Swiss competition law (cf. Art. 5 sec. 1 of the Swiss Federal Cartel Act and paragraph 12 (g) of the corresponding Vertical Agreements Directive). Even though the applicable directive is not statutory law and does therefore not officially bind courts, it must be assumed that the latter will take it into account when ruling on the validity of a non-competition clause.

VI. Trade Mark Registration and License Agreement

If a registered trademark is involved in the cross-border distribution, the manufacturer/supplier must be aware that such trademark is not necessarily protected in the targeted distribution territory. Thus, it is very important to initiate the required registration procedure on time.

A. Trade Mark Registration

Under Swiss law, trademark rights are subject to federal law (Federal Act on the Protection of Trade Marks) as well as international treaties. Any graphics, words or single letters, three-dimensional forms, slogans or even series of tones (acoustic trademark) can be used and protected as a trademark. But trademark protection in Switzerland, like in most other countries, only arises with its prior registration with the Swiss Institute for Intellectual Property ("IGE"). The registration of a trademark gives its owner the exclusive right to use the trademark for the goods and services for which it has been registered. Thus, any third party is prohibited by law from using or registering the same or a similar trademark for such goods and services without being licensed by the trademark owner.

The duration of the registration proceeding depends on the particular circumstances. At best, the application will be examined within 10 working days and the trademark can be registered as soon as the fees are paid. The

trademark registration fee for 10 years and three classes of goods and/or services is CHF 550. After 10 years, the registration can be renewed as many times as required. However, if the registered trademark is not used for a consecutive period of more than five years, it might lose its protection.

Trademark protection is generally limited to the country of its registration. The Madrid system for the international registration of trade marks, based on the Madrid Agreement and the Madrid Protocol, offers a trade mark owner the possibility to have his trade mark protected in several countries by filing only one application with his own national trade mark office. Among nearly 90 other states, China and Switzerland are both members of the Madrid Union.

B. License Agreement

If a local agent or distributor shall be entitled to use a registered trade mark within his distribution activities, a license agreement should be concluded. The Swiss CO does not contain any provisions regarding license agreements so that its conclusion does not require any specific formalities. Nevertheless, a written contract is advisable in any case. Generally, there are two different types of license agreements, i.e. exclusive and non-exclusive. If the parties agree upon an exclusive license agreement, the licensee is granted an exclusive right to use the trademark, otherwise the licensor keeps the right to conclude further license agreements with third parties.

It is important to specify in which territory and for which kind of activities the licensee shall be entitled to use the trademark. The term of a license agreement is automatically limited by the term of the underlying trademark right. If the license right may be terminated before, this must also be stated in the license agreement.

VII. Other fields of law to keep in mind when establishing a distribution system

A. Competition Law

Swiss as well as European Law provides for several restrictions on *vertical agreements* in order to guarantee fair competition. Vertical agreements are defined as formal or informal undertakings between companies of different market levels fixing terms of purchase, sale or resale of goods and services, and therefore also include distribution agreements. Pursuant to these restrictions, it is forbidden for a supplier to establish minimum or fixed prices in a distribution agreement. On the other hand, the establishment of maximum prices and price recommendations is permitted. The demarcation between fixing and recommending prices can however lead to difficulties and will be on the discretion of the competent competition authority or court.

An illegal elimination of competition is further assumed if a distribution agreement allocates territories in a way that prohibits not only active, but also passive sales into another territory. A passive sale is a sale based on an unsolicited request by a customer from outside the territory allocated to the distributor. Under Swiss law, breach of competition law may be sanctioned with a fine of up to 10% of the turnover realized in Switzerland in the last three years.

Nevertheless, under certain circumstances vertical agreements as mentioned above are not deemed to eliminate fair competition. For instance, if an agreement is essential to decrease production and distribution costs or to optimize production processes, it will not be considered illegal according to the Swiss Federal Cartel Act.

B. Product Liability

A manufacturer selling or exporting products into Switzerland must be aware of the applicable Swiss laws regarding Product Safety and Product Liability. Both statutes apply to manufacturers as well as importers and oblige them to meet particular requirements with regard to the safety of their products. The

Swiss Product Liability Law further provides for the manufacturer's liability for personal injury or property damage caused by a defective product. This is a liability based on causality, which means that the manufacturer's right to raise objections is very limited.

C. Applicable Law

According to Swiss International Private Law, any kind of distribution contract (agency, commission, brokerage, or distribution agreement) is governed by Swiss Law if the party performing the characteristic obligation of such contract (i.e. agent, commission agent, broker and distributor) is domiciled in Switzerland and the parties have not explicitly chosen the law of another country. For a supplier concluding a distribution agreement it is however important to note that if the parties to a distribution agreement do not explicitly exclude its application, questions regarding the purchase part of the distribution agreement will be governed by the CISG (United Nations Convention on Contracts for the International Sale of Goods). Therefore it is advisable to appoint the applicable law in the written distribution agreement.

VIII. Conclusion

Distribution through agents, commission agents and brokers gives the supplier the advantage of keeping control over the distribution, including sales prices. As the position of an agent is rather close to the one of an employee, agency agreements are however subject to several statutory regulations. The conclusion of a distribution agreement, in contrast, generally allows the parties to freely negotiate its terms and conditions and to transfer the distribution risk to the distributor. In addition, a distribution agreement usually facilitates the installation of a highly efficient distribution channel because the distributor has an own interest in the establishment and maintenance of a well functioning distribution. Nevertheless, the supplier must be aware of certain provisions ruling the agency agreement (e.g. inalienable goodwill payment) that might, under certain circumstances, also apply to a distribution agreement. Finally, before the conclusion of a distribution agreement, potential competition law infringements need to be considered carefully.

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