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LAW FIRM

House of Lords settles long-standing debate on payments to commercial agents following termination of contract

Following termination of a commercial agency contract by a supplier, the agent is entitled to “compensation” for the loss of business that derives from the termination in accordance with the UK Commercial Agents (Council Directive) Regulations 1993, which is the legislative embodiment here of the European Directive that provides the European law on the subject.

The House of Lords in *Lonsdale v Howard & Hallam Ltd* has recently decided a long running debate as to the manner in which the “compensation” is calculated. The British court has turned away from the more generous measure of compensation which is payable in other European jurisdictions, particularly in France, and applied a dose of British realism to the calculation. It has determined once and for all the principles that set the measure of compensation here.

Background to the case

The Claimant, Mr Lonsdale, was a self-employed agent in the shoe trade. Howard & Hallam were suppliers selling a brand of shoes for which Mr Lonsdale was the selling agent. Following a decline in sales, Howard & Hallam ceased trading in 2003. The brand was sold to another supplier. As a result, Mr Lonsdale was given six months notice of the termination of his agency. He was given commission on the sales that he had by then generated. He was also paid £7,500 as “compensation”.

Mr Lonsdale, on advice, believed that this was insufficient “compensation” for the loss he suffered. He started an action in the Oxford County Court.

Calculating the compensation

The action took place against differing views as to the way in which compensation should be calculated. In France the method of calculation is to take as a starting point twice the average annual gross commission over the previous three years. This method of calculation was said to have some support from the European Commission’s report on the application of the Directive.

The Oxford County Court rejected these arguments and in particular that as a starting point there was an automatic assessment of damages based on the French method of calculation. It confirmed that Mr Lonsdale was entitled to be compensated for the goodwill that he held in his agency and the damage caused by the termination of that agency but that value should be calculated on the basis of a hypothetical sale between willing seller and willing buyer. There was, however, no valuation evidence before the court and the judge rather plucked out of the air a figure of £5,000. Since £7,500 had already been paid, Mr Lonsdale recovered nothing further.

The matter went to the Court of Appeal who confirmed the judge’s view, although it did suggest that the parties should have provided expert evidence of valuation for the County Court.

Such was the importance of the principles involved in calculating the damages that the matter found its way up to the House of Lords. Lord Hoffman delivered the judgment of that Court.

Lord Hoffman analysed the law and the differing methods of calculation. He accepted that the compensation should be based upon the loss of the value of the agency which has been terminated. The agent was deprived of his right to future commissions and that was what was to be compensated under the Directive and Regulations.

The most important issue, however, was the method of calculation. The judgments of the County Court and the Court of Appeal had rejected the French method of calculation as some automatic means by which compensation should be measured. Lord Hoffman agreed. He determined that the method which should be adopted was to analyse in each case what a hypothetical purchaser would have paid for the agency. Clearly if the goodwill of an agency were to be marketed and sold, the purchaser would be looking at the ongoing commissions that were likely to result from the agency as a business.

The outcome

For Mr Lonsdale this was bad news because Howard & Hallam had ceased trading and therefore the agency was going to terminate in any event. Further, the sales were declining which was the reason behind its closure. There was no ongoing business for which any hypothetical purchaser would pay.

Accordingly, in this particular case the court thought that the £5,000 ordered by the County Court judge for an agency in decline was a generous figure. Lord Hoffman refused to interfere with the award but suggested that the County Court judge could well have simply dismissed the claim.

Thus Lord Hoffman established the principle on which a valuation for compensation purposes in accordance with the Commercial Agents Regulations must be undertaken – what a hypothetical willing purchaser would pay for the goodwill of the agency in the given circumstances for each case, taking as its date the date of termination. The sums may generally not be large and Lord Hoffman expressed the view that they could probably be agreed in most cases now that he had established the principles involved. Perhaps this optimistic view will be fulfilled, although the scope for differences on valuations is clearly very significant.

What does this mean for the supplier and the agent?

In the event of the supplier terminating their business or the business being in decline, then it will severely reduce the amount of compensation that will have to be paid under the Directive and Regulations. If, however, sales are on the up, then this is likely to increase the valuation. Good and bad news for both sides of the equation.

It seems unlikely that this will be the end of litigation on the subject but now that the House of Lords has opined on the principles, the argument will be between two expert valuers applying those principles.

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