



# Commercial Services

## Appointing Commercial Agents

Any business appointing a commercial agent to sell goods on its behalf within Great Britain should be aware of the Commercial Agents Regulations which afford various rights to commercial agents. Ensuring an awareness and understanding of the Regulations as well as having a robust commercial agency agreement in place from the outset of the agent's appointment is vital in order to minimise risk on what can prove to be costly termination exercises at the end of the agency relationship.

### What do the Regulations cover?

The Regulations set out various rights as well as obligations which apply to commercial agents and their activities. A commercial agent is defined under the Regulations as a self employed intermediary with the continuing authority to negotiate the sale or purchase of goods on behalf of a principal. The definition covers both individuals and companies acting as agents.

The rights afforded to a person falling within this definition cover a number of points. For example, the Regulations prescribe minimum notice periods due to agents on termination of their appointment, stipulate rules about an agent's entitlement to commission on sales made and set out duties owed by a principal to his agent and vice versa.

### The cost of termination

It is however, the rights of commercial agents on termination and their entitlement to claim a termination payment which present greatest commercial and financial risk to a principal if left unaddressed.

The Regulations make clear that a commercial agent is entitled to either be indemnified or compensated after termination of the agency arrangement. They also make clear that unless the agency agreement specifically provides for an indemnity payment, compensation as the default position, will instead apply.

Termination circumstances which can give rise to claims are wide and include termination due to retirement or illness of the agent, where a fixed term appointment expires and where a principal terminates the agreement at will without any serious breach of the agreement by the commercial agent.

### Indemnity or Compensation?

An indemnity payment is subject to a maximum formula prescribed in the Regulations as an amount not to exceed one year's average annual remuneration over the preceding five years. Whilst obviously at the time of appointment of a commercial agent, this figure will not be known to a principal, an indemnity has the advantage of being a clearly prescribed formula which is not only relatively straightforward to calculate but also gives the principal a degree of certainty. For these reasons, selecting an indemnity mechanism in the contract is often seen as a favourable option for those who appoint agents.



The compensation entitlement is more complex. The Regulations do not prescribe a formula and instead, this method has been left for the Courts to determine. The current position is prescribed by the case *Lonsdale v Howard & Hallam Ltd* which stipulates that compensation is calculated by reference to the value of the agency business at the time of termination, including the value of the goodwill.

This marks a shift away from previous methods of calculating compensation and has an obvious lack of certainty on what the termination payment may amount to at the end of the relationship, especially as it is impossible to foresee what the circumstances will be at that time. In addition, specialist accountancy advice is also likely to be necessary in order to determine the value attributable to the business so leading to additional cost.

Of course, if an agency business performs poorly, the amount of due compensation may be relatively low. However, the risk of costly and potentially complex claims from strong agency businesses means that the level of exposure for principals is potentially unlimited.

### **The need for an agency agreement**

Whilst many of the rules in the Regulations are mandatory and indeed liability for termination payments cannot be removed, it is essential to minimise risk and potential cost with a clear and effective agency agreement (to which an agent has a regulatory entitlement in any event). This is vital not only to give contractual certainty and protection as with any other commercial arrangement but entering into the agreement at the time of agency appointment is crucially, the stage at which the effect of the Regulations must be taken into account.

More often than not, the agency contract will involve a principal who appoints a commercial agent, opting for an indemnity as the preferable method of termination payment calculation. However, this is just one issue to address in an agency agreement which should cover other key issues such as clarity on when and how much commission is payable and the scope of agency activity and responsibility through the appointment.

### **Who to contact:**

For advice or further information about how we can help you please contact:

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