

# **SALES AGENCY RELATIONSHIPS UNDER UNITED STATES LAW**

**1. TERMINATION AND NON-RENEWAL  
BY THE PRINCIPAL: INDEMNITIES  
AND DAMAGES**

**2. OTHER POTENTIAL PROBLEM AREAS**

**----A SHORT GUIDE FOR THE FOREIGN  
BUSINESS PERSON---**

**By**

**AARON N. WISE**  
Attorney at Law  
Member of the New York Bar

**AARON N. WISE, ESQ., PARTNER**  
**Gallet Dreyer & Berkey, LLP**  
**Attorneys at Law**  
**845 Third Avenue, 8<sup>th</sup> Floor**  
**New York, New York 10022-6601**  
**Telephone: (212) 935-3131**  
**Telefax: (212) 935-4514**  
**E-mail: anw@gdblawn.com**

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### **About the Attorney-Author**

**Aaron N. Wise** is a partner of the New York City law firm Gallet Dreyer & Berkey, LLP LLP. Mr. Wise's areas of expertise include corporate, commercial and contract law, taxation, intellectual property law, and litigation and arbitration,. Mr. Wise holds law degrees from Boston College Law School, New York University Law School and the University of Paris (France). He is a frequent lecturer inside and outside the USA and is listed in *Who's Who in the World*, *Who's Who in America* and *Who's Who in American Law*. Mr. Wise is proficient in French, German Italian, Spanish, Portuguese, Russian and Japanese, and has a basic working knowledge of several other languages. He also practices in the sports law field, both domestically and internationally. He is the author of the multivolume work, ***International Sports Law and Business*** (Kluwer Law International, The Hague and Cambridge, Mass., 1997). He has been a speaker at seminars held both inside the USA and in and many foreign countries on doing business in the USA and on sports law and sports business topics. Mr. Wise has considerable experience in representing foreign companies and individuals in connection with their U.S. and international legal and tax matters; and U.S. companies with their foreign and international ones.

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### **Other Cost-Free Publications of this Attorney-Author**

See the **Annex 2** to this Guide.

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### **PART I. TERMINATION AND NON-RENEWAL BY THE PRINCIPAL OF SALES AGENCY CONTRACTS AND RELATIONSHIPS: CAN THE PRINCIPAL BE LIABLE FOR AN INDEMNITY OR DAMAGES**

#### **Introduction: What is a “Sales Agent” under U.S. Law and Practice?**

In this Guide, we are dealing only with “sales agents” in regard to the main issues covered : (i) termination and non-renewal of the sales agency contract by the principal and whether the sales agent can claim an indemnity or damages should that occur; and (ii) some other potential problem areas involving sales agents.

Under U.S. law and practice, a “sales agent” does not purchase and resell goods from its principal. If the principal is selling mainly services to its customers, the sales agent does not render the services in its own name and for its own account to the customers---and typically, does not render them at all. Rather, it is the principal that sells the goods and services (and renders them) to the customers. The contractual relationship with the customers is with the principal, as the seller of the goods and services. The “sales agent” generally seeks to obtain and obtains orders from customers and passes them on to its principal for acceptance (or rejection) and fulfillment. Typically, the sales agent will have a contractually assigned territory, in which it can solicit and obtain orders. That territory may be, for the sales agent, an exclusive, quasi-exclusive or non-exclusive one,

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depending on what the contract provides (written one, or, to the extent enforceable, oral one), and on the intent of the parties and what the course of conduct between them has been. The sales agent will typically be entitled to a commission from the principal for sales of the principal's goods or services (as agreed between them) generated by the sales agent, or, sometimes, from all sales made in the sales agent's territory even if the sales agent did not actually take or generate the particular order(s) or originate the particular customer.

A "sales agent" can be a legal person (e.g., a legal entity) or an individual. Sometimes, a "sales agent" is called, in U.S. parlance, a "sales representative" or a "sales rep".

A distributor or dealer (for purposes of this Guide, these two terms are used without distinction) buys and resells in its own name and for its own account, the products of its supplier. Or, if the supplier is selling services to customers, the distributor/dealer will sell those in its own name and for its own account. A distributor or dealer will normally not receive any commission from the supplier; rather, it receives its profit from the resale (or sale, in the case of services) of the supplier's goods or services. An enterprise marketing computer software might appoint one or more "authorized resellers" to sell software licenses and services. The reseller is a combination of master licensee/distributor, and will normally split the resulting revenues in various ways with the software supplier.

Once again, the focus of this Guide is 1. whether, under American law and practice, a terminated sales agent can, through its lawyer, make reasonably good arguments that it is entitled to damages for improper termination of his contract or relationship by the principal; and 2. some other potential problem areas under American law relating to sales agents.

Other than a few comments, we do not deal with these issues as they may apply to distributors, dealers, licensees and franchisees.

### **U.S Federal and State Legislation, Case Law and Principles regarding the Sales Agent Termination/Non-renewal Issue**

There is no U.S. federal law that specifically accords a terminated or non-renewed sales agent a right to damages or an indemnity or damages. It will be the law of one or more particular U.S. states (state law) that will determine these issues.

In most American states and territories, there is no legislation dealing specifically with the termination or non-renewal of sales agency contracts and relationships or whether the sales agent is entitled to any damages or indemnity due thereto.

One important exception is New York State, which has a law applying specifically to "sales representatives", a defined term that is essentially the same as a "sales agent". A brief summary of that law is in *Annex 1*. *If you, the reader, have or likely to have a*

*“sales representative” or “sales agent” whose territory is or will include New York State, then Annex 1 is clearly recommended reading.*

Another exception is the Commonwealth of Puerto Rico, which has legislation dealing with the termination and non-renewal of both sales agents and distributors/dealers. The Puerto Rican legislation entitles a sales agent, as well as distributor or dealer, whose contract or relationship is terminated by the principal or supplier without “just cause” (as defined in the law) to an indemnity (damages).

However, the law of many, if not most, other U.S. states may provide for the basis for a claim for improper termination of a sales agency. A reasonably clever American lawyer can often find one or more—typically, several--- legal theories on which to base such a claim. The lawyer will often find some generally worded state law(s) that will support a claim. But mostly, it will be case law (court decisions) that will provide the main ammunition for such arguments.

Two main thrusts of such claims will often be, particularly where the termination is without good cause:

- The sales agent has generated business (customers), thus continuing profits for the principal after the sales agency ends. The principal’s termination or non-renewal will cause the agent to lose future commissions and good will and will unjustly enrich the principal;
- The sales agent has invested considerably moneys in the sales agency, and the termination or non-renewal will not give the sales agent the opportunity to recoup that investment. That point will often turn on whether the principal has given the agent a notice of termination or non-renewal sufficiently long to give the agent the possibility of recouping its investment in the sales agency or to find one or more new sales agency relationships to replace it.

There may well be other general theories that the agent’s lawyer can invoke.

In some U.S. states, there is an “implied covenant of good faith and fair dealing” imposed on each party to a contract. That means that each party to a contract (whether written, oral, one created by conduct or correspondence, etc.) must act in good faith and deal fairly with the other party. Here, we are speaking of the principal and the sales agent as the parties. A claim for improper termination or improper non-renewal might be based on this implied covenant. Even if a written contract exists providing for termination without cause or even for a specified cause by the principal, and if termination is based on the contractual provision, the “implied covenant” might be raised to claim that that termination (or non-renewal) was motivated by and done in bad faith by the principal, and would unfairly deprive the sales agent of future benefits which it reasonably could expect from the relationship.

New Jersey is, for example, one State that applies the “implied covenant of good faith and fair dealing” to all contracts subject to New Jersey law, including sales agencies.

California law is another to avoid to the extent possible.

New York State law generally does not apply any such “implied covenant” or any similar legal principle---particularly one likely to override specific termination and other clauses in a written contract.

There is absolutely no substitute for a very well thought out and drafted contract, U.S. style, prepared by an American lawyer, that protects his/her clients interests. That applies to a sales agency or any other type of contract. Such a contract will reduce very substantially the risks of a claim for improper termination or non-renewal by the sales agent. The principal's U.S. lawyer would, among other things, want the contract to be governed by a U.S. state's law, like that of the State of New York. As stated, New York state law normally will not permit a damage claim for improper termination or non-renewal of a sales agency that was based on the specific terms of the written contract---even a clause permitting termination without cause. New York law generally tends to allow the parties to enforce the contract as written, as between business people.

There is the New York State “sales representative” statute (see summary in Annex I). But that law will apply anyway to sales representative agreements if the criteria for its application are met, and the principal will have to comply with it; and, it is not a law according the sales representative an indemnity for improper termination or non-renewal. The fact that New York law is stipulated in the contract as the applicable law will not cause that law to apply or not apply to a particular “sales representation”---the particular criteria set forth in that law will. Thus, that New York State law's existence is no reason not to provide for the application of New York State law in the sales agency contract, assuming there are no other reasons for not doing so.

The principal, through its lawyer, should at all times maintain the drafting initiative---it should prepare the contract drafts and not allow the sales agent or its lawyer to prepare any contract drafts, but only to comment/propose changes to the principal's drafts. That will usually result in a contract that properly protects the principal's interests.

Just for purposes of example, assume a non-US “principal” ---a company in France, that intends to engage a sales agent or sales representative in the USA. While the French company might, at first blush, like to state in the contract that French law applies to it (and state as well that French courts or a particular French court will resolve all litigation), that is not normally advisable. French law clearly provides for an indemnity on termination of sales agents. If the law applicable to the contract were stated to be French law and if the matter came before a French court, there is a good chance that the French court would accord the agent an indemnity based on the French legislation. The same is likely to occur if the matter came before an American court or even an arbitration

panel (wherever located). There are several other reasons that provisions of that type are not advisable for a foreign company from any country.

Normally, the best solution for a foreign principal, in a sales agency contract involving the U.S. market, would be to provide in the written contract for the applicability of a U.S. state law, e.g., like that of the State of New York, which normally will apply the terms of a written contract and not be favorable to damage claim for improper termination or non-renewal. There are a several other reasons why it may be beneficial for the principal to stipulate the law of a favorable U.S. state in the contract.

That might be coupled with a clause providing for arbitration of disputes and claims arising under the contract within the same particular U.S. state mentioned in the preceding paragraph, for example, if the applicable law were specified as New York law, the arbitration could be in New York City, the headquarters of the American Arbitration Association (“AAA”).

There are a number of other clauses that a foreign principal desiring to protect itself against improper termination/non-renewal claims, and other potential claims, should typically include in the written contract. See the next subsection.

#### **Examples of Clauses Designed to Protect the Principal against Sales Agent Termination/Non-Renewal Claims**

Here are some of such clauses:

1. various specific clauses allowing the principal to terminate for cause. For example, the sales agent’s failure to obtain a specified minimum orders amount within the agreed time period; termination due to the agent’s breach of the sales agency contract or tortious conduct by the sales agent; termination for certain changes of circumstance (e.g., the agent ceasing to do business or liquidating, if a company; or change of key personnel or control of the agent company).
2. clauses allowing the principal to terminate without cause on a specified amount of prior notice.
3. clauses stating that there will be no liability to the principal (or either party) due to the termination or other ending of the contract and relationship in accordance with the contract’s terms and applicable law [That would not apply to moneys actually owed by the principal to the agent such as for commissions already accrued up to the contract’s end, or by the agent to the principal such as for advances against commissions in excess of commissions actually earned].
4. clauses stating that both parties agree that the termination and termination notice provisions contained in the contract are reasonable, are not unconscionable or otherwise unfair and that neither party will ever so claim; that the contract is a negotiated one

between equals; and that both parties are the drafters of the contract so that no presumptions against the drafter will apply.

5. clauses providing for, as applicable law, the law of a US state that is reasonably favorable to the supplier regarding termination and non-renewal issues (see above).

6. a well thought out, properly drafted arbitration clause. Legally, there should be a reasonable connection between the U.S. State, the law of which is chosen to apply to the sales agency contract, and the overall transaction or one or more of the parties. So, for example, imagine a sales agency contract between a non-U.S. (e.g., French) principal and a sales agent with its business or residence in a U.S. State other than, for example, New York State. If New York State law were made the applicable law, it would be preferable to provide for arbitration of all disputes somewhere in New York State (e.g., in New York City, under the AAA International Arbitration Rules). Linking the New York arbitration clause with a New York State applicable law clause should be a sufficient reasonable connection.

7. a clause stating that no conflict of laws (the French call it “private international law=droit international privé”) doctrine will apply that will result in the law of any other jurisdiction being applied in place of the one stipulated in the contract (a U.S. state’s law favorable to the principal).

For example, France (as does many other countries) has a law protecting commercial agents by way of indemnity on termination. Let us assume that the sales agency contract between the French principal and the U.S. sales agent states that New York State substantive (material) law will govern it, its performance, termination etc.

There is a legal principle that some American courts have applied to distributor, dealer and sales agency termination that might lead to a court or arbitrator to disregard the (for example) New York State applicable law provision and apply some other law. In this hypothetical example of a French principal, that law might be French law—and in particular, the French law granting the sales agent an indemnity on termination. That legal principle is very roughly like this:

(i) if the parties have specified an applicable law in their contract and that law has a reasonable relationship to the transaction as a whole, then the selected law will apply;

but notwithstanding that

(ii) if there is a jurisdiction with a materially greater interest in the determination of a particular issue and that law would apply to that issue if there were no specified applicable law in the contract, then that other jurisdiction’s law will apply to it.



The terminated or non-renewed principal could argue: (i) despite the contract's clause stating that New York State law applies, France, the location of the principal, has a materially greater interest in determining the agent's termination indemnity claims; (ii) French law would be applicable (at least to that issue) if the contract did not contain the New York State law clause; and (ii) thus, French law applies—for example, its law on commercial agents granting the agent an indemnity on termination or non-renewal.

I have seen and have represented clients in just such situations, involving suppliers from several countries.

In the sales agency contract, clear and specific provisions should be included that make it clear that the above legal principle—disregarding the contractual applicable law clause and shifting it to another law (e.g., that of the principal's country)--- will not apply. That principle is not mandatory U.S. law and probably can be avoided by such contractual language.

There are other clauses that the contract might contain to reduce the principal's risks that will not be mentioned here.

Many of the points and suggestions made above apply where the “principal” is the US subsidiary or US affiliate of a foreign company.

### **What the Principal Should Not Do; and What the Principal Should Do**

The principal should definitely avoid the following with regard to sales agencies for the U.S. market:

1. having no written contract, only an oral one;
2. having a de facto sales agency relationship;
2. having only correspondence that establishes a contract with the sales agent;
3. having a sales agency contract that is not prepared by an experienced American lawyer.

Oral and de facto sales agency contracts, and those that result from normal correspondence or memoranda, can be valid under American law. Sometimes, for example, a “de facto” sales agency relationship under which the principal only uses one sales agent, may result in that agent being considered, legally, the principal's exclusive sales agent for the entire USA.

These are the types of contracts and relationships that most often result in claims against the principal and litigation, including for improper termination or non-renewal. And, these are the type of cases that often, the principal will lose.

The reader should bear in mind that the great majority of commercial lawsuits (or threatened ones) in the USA end up in a settlement between the parties. The terminated or

non-renewed sales agent may threaten to bring, or actually bring, a lawsuit only to pressure the principal into concluding a settlement for a considerable amount of money paid to the agent. The principal, particularly one in another country (e.g., France), may be intimidated by the amount of damages that the sales agent may claim (or possibly recover) and by the costs of fighting a litigation (or even arbitration).

Most often, a properly drafted contract (as described above) will be a good protection against such a situation.

### **Termination of Distributors, Dealers and Licensees: Damages and Indemnities under U.S. Law**

While this is not the subject matter of this Guide, a few remarks are in order.

A great many of the points made above will apply to the termination of distributors, dealers and licensee under U.S. law. There are some differences, however. There are few U.S. federal statutes that apply to the termination of certain types of distributors and dealers. Also, in a few U.S. states, there are specific laws dealing with the termination of distributors and dealers. There are as well certain provisions of the U.S. law of sales (which is a unified law applicable in all U.S. states, with some minor differences) containing general principles that might be used to attempt to justify improper termination claims by distributors, dealers and licensees. In addition, most U.S. states have “franchise acts”---specific laws applicable to franchisor-franchisee relationships. Some of those franchise acts and the pertinent case law will characterize certain distributorship, dealership and license contracts as being “franchise contracts” subject to its franchise act. Some of those state franchise acts prohibit the franchisor from terminating the franchise other than for “good cause”, which is often a rather narrowly defined term; and provide for multiple damage claims (e.g., 2 times or three times the damages claimed).

The reader should not be confused. The preceding paragraph does not apply to “sales agency” contracts and relationships.

But again, as in the case of sales agents, well conceived and drafted contracts, prepared by a competent and experienced U.S. lawyer, can usually reduce the supplier’s risk of improper termination claims and other potential ones by its distributor, dealer, or licensee.

## **PART II. OTHER POTENTIAL PROBLEM AREAS REGARDING SALES AGENTS**

I will mention a few other points to bear in mind in connection with sales agency contracts and relationship for the U.S. market.

1. **Commission, Rate and Basis:** These terms must be carefully negotiated and drafted. On which sales does the agent or sales rep earn its commission and at

what point in time? If you have more than one sales agent or rep for the USA, there is the potential for territorial customer overlaps. Who earns what commissions on which sales are questions that should be resolved in advance by contract.

2. **Agent or Rep Accepting Orders:** Avoid allowing your sales agents or reps to have the power, or to exercise the power, to accept orders for your goods (or services). Allowing any of your agents to accept orders can result in U.S. tax and legal problems for you. You, principal, should be the only one to accept (or decline) orders. Those points should be clearly specified in the sales agency contract; and the principal should, in actual practice, adhere to them.

3. **Advances :** If you, the principal, plan to allow your agent or sales agent or rep to receive advances against future commissions, the contract should be very clear that these are advances to be repaid within a specified time--even if earned commissions do not equal the advances.

4. **Rep or Sales Agent as Your Employee:** If your sales rep or agent is an individual, take care that he/she is not legally characterized as your "employee". Simply writing in the contract that he/she is not your employee will probably not do the trick. There are specific American rules governing when an individual is or is not the "employee", rather than an independent contractor. If, in fact, the individual should successfully claim he/she is an employee and certain payments should have been made to him or on his behalf by the "employer" that were not made, the "employer" will have a serious problem. Even if the sales rep or agent functions as such through a company he/she owns (which is the contracting party), rather than as an individual, this danger may possibility may still exist, depending on the circumstances.

Also, for income and other tax reasons, a foreign company will not want to have any U.S. employees soliciting and taking orders for good or services on its behalf within the United States.

A foreign company (or its US subsidiary or affiliate) should consider not engaging any individual (physical person) as its sales agent or rep that it does not want to be its "employee", but rather, engaging only companies (legal entities) meeting certain conditions as its sales agents. If, after checking with your American legal counsel, it seems that one or more sales reps or agents are, in fact, likely to be viewed as your employees, and if you cannot alter that situation, you should consider forming a U.S. subsidiary and having those individuals be employees of the subsidiary.

5. **Rep or Sales Agent of Your US subsidiary or affiliate company:** If a foreign company either already have or about to form a US subsidiary or US affiliate company, it will normally be preferable to have the US sales reps or agents be the rep or agent of your US company, not of the foreign company. The contract with the rep or agent should so state. And the foreign company already has a US agent or rep, the latter should be switched over to being such for the US subsidiary affiliate, in a contract so stating. There may be exceptions to this, as there is for most things.

## **ANNEX 1: SUMMARY OF NEW YORK STATE'S LAW APPLICABLE TO "SALES REPRESENTATIVES"**

New York State has a law concerning "sales representatives", a term defined in the law. A "sales agent" meeting that definition would also qualify. A "sales representative" is defined as an individual or a legal entity which solicits wholesale orders in New York State on behalf of a "principal", is paid on a commission basis, and is not an employee of the principal.

The New York law defines "principal" as "a person or company engaged in the business of manufacturing, and who (i) manufactures, produces, imports, or distributes a product for wholesale; (ii) contracts with a sales representative to solicit orders for the product; and (iii) compensates the sales representative in whole or in part by commissions.

In summary, the law provides

(1) Where the sales representative is to solicit wholesale orders in New York State, there must be a written contract between the principal and sales representative setting forth the method by which the sales representative's commission is computed and paid;

(2) The principal must provide the sales representative with a signed copy of the contract and must obtain a signed receipt for it from the sales representative;

(3) The sales representative must be paid his/her/its earned commission under the contract in accordance with its terms, but not later than 5 business days after the commission is earned (the term "earned commission" is defined in the law); and if the sales representative contract becomes terminated, within 5 business days after termination or within 5 business days after the commissions become due in the case of earned commissions not due for payment on the sales representation contract termination date;

(4) When the sales representation contract ends, all "earned commissions" must be paid to the sales representative at the usual place of payment unless the representative requests that commission payments be sent by mail, and if sent by mail, the earned commissions are deemed paid as of the date of postmark; and

(5) A principal that fails to comply with that law's provisions on timely payment of all "earned commissions" is liable for "double damages"; and the winning party in litigation (and presumably, arbitration) is entitled to recover its reasonable attorneys' fees, court costs and disbursements.

As stated above, if the person concerned is really an "employee" of the other party, and not a sales representative (which is an independent contractor), then this law does

apply. Rather, New York State's provisions in its labor law will apply if the person is employed in New York State will (along with US federal employment laws and possibly, labor laws).

*The reader should note that this New York State law is not one that accords the sales representative an "indemnity" or damages for improper termination or non-renewal.*

There are several aspects of this New York State sales representation law which are unclear. In particular situations, it might not be 100% clear if it applies.

## **ANNEX 2: LIST OF OTHER NO COST PUBLICATIONS OF THE ATTORNEY-AUTHOR**

Unless otherwise stated, the author of the cost-free publications below is Aaron N. Wise, Attorney at Law and partner of the law firm, Gallet Dreyer & Berkey, LLP à New York City, USA. These (and others) can be obtained by contacting Mr. Wise or by downloading them from his law firm's website, [www.gdblaw.com](http://www.gdblaw.com), by, on the home page, clicking "Practice Groups" and on the next screen, "International" and right under that, "Publications".

Doing Business in the USA" a "Bullet Point" Guide....." (available in English and several other languages).

What Type of American Legal Entity Should I Use for my American Business Operation ? A Guide for the Foreign Business Person

A Foreign Business Person's Guide to American Law – Business Practices - Taxation

American Product Liability: "Good News for Business!" Recent Trends and Developments: A Guide for Foreign Companies

General Terms of Sale for Exports to the USA, the Western Hemisphere Generally and Worldwide: A Guide for the Foreign (non-US) Exporter

Placing Your Goods "on Consignment" with your American Business Partner: What the Foreign Exporter and its Financing Bank or Factor should know

Debt Collection: Will United States Court Recognize and Enforce Foreign Country Judgments? A Practical Guide for the Foreign Lawyer and Business Person

Dealing with Employees under American Law: A Short Guide on Some Important Points

Purchase and Leasing of Real Property in the United States  
(the authors are David L. Berkey, Partner, and Aaron N. Wise, Partner, Gallet Dreyer & Berkey, LLP)