

## **Lonsdale v Howard & Hallam Ltd<sup>1</sup> ~ the End of the Road**

**By Fiona Banks<sup>2</sup>  
July 2007**

The House of Lords has recently handed down judgment in *Lonsdale*, a case concerning an agent's right to "compensation" for termination of a commercial agency pursuant to Regulation 17(6) of the Commercial Agents (Council Directive) Regulations 1993.<sup>3</sup> Lord Hoffmann, with whom all of the Law Lords agreed, considered that an agent is entitled to be compensated for being deprived of the benefit of the agency relationship. The valuation of that loss is to be reached by analysing what could reasonably have been obtained, at the date of termination, for the rights which the agent had been enjoying.

### **Facts and arguments on appeal**

Mr Lonsdale works as a commercial agent in the shoe trade. From 1990 until June 2003, he acted as agent for Howard & Hallam, the Defendant company, selling their Elmdale brand of shoes in South-East England to shoe shops. After a decline in sales for several years, Howard & Hallam ceased trading in 2003 and the goodwill of the Elmdale brand was sold to a competitor.

Howard & Hallam gave Mr Lonsdale six months' notice of the termination of his agency and he was paid the outstanding commission on the sales that he generated. Mr Lonsdale was also paid £7,500 as compensation pursuant to Regulation 17(6). Mr Lonsdale considered this to be inadequate compensation and therefore brought a claim in the Oxford County Court.

The judge at first instance held that Mr Lonsdale was entitled to be compensated for the goodwill that he possessed in the agency. However, given the absence of valuation evidence, or evidence that anyone would be prepared to buy the agency, the judge settled on a figure of £5,000.

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<sup>1</sup> *Lonsdale v Howard & Hallam Limited* [2007] UKHL 32, judgment 4 July 2007 (Lord Bingham of Cornhill, Lord Hoffmann, Lord Rodger of Earlsferry, Lord Carswell, Lord Neuberger of Abbotsbury)

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<sup>3</sup> Implementing Council Directive 86/653/EEC on the co-ordination of the laws of the Member States relating to self-employed commercial agents (the 'Directive')

The Court of Appeal approved of this approach and declined to interfere with the amount of the award. The Court noted that in most cases expert witness evidence, on the appropriate way of valuing the business, would be necessary.

Before the House of Lords, it was argued on behalf of Mr Lonsdale, that the common practice of the French courts in valuing agencies at twice the average annual gross commission over the previous three years, subject to variation in exceptional cases, should be adopted. It was submitted that Article 17(3) of the Directive (implemented domestically by Regulation 17(6)) adopted the French practice as Community law and that therefore the French method of calculating compensation should be followed. This, it was argued, had been indorsed by the Commission's report on the application of Article 17 ('the Report').<sup>4</sup> If this was not accepted as the plain and obvious meaning of the Directive, it was urged that the question should be referred to the European Court of Justice. Counsel for Howard & Hallam submitted that in all the circumstances the figure of £5,000 was fair and reasonable and should be allowed to stand.

### **Judgment of the House of Lords**

Lord Hoffmann, in addressing the first issue of exactly what the agent should be compensated for, found the Directive to be explicit. The agent is entitled to be compensated for "*the damage he suffers as a result of the termination of his relations with the principal.*" The agent has been deprived of his right to future commissions and it is the loss of this right for which the Directive requires the agent to be compensated.

The second issue concerned how that loss should be calculated. Lord Hoffmann considered that, like any other exercise in valuation, this requires an analysis of what could reasonably have been obtained, at the date of termination, for the rights which the agent had been enjoying. A necessary assumption in this analysis is that the agency would have continued and the hypothetical purchaser would have been able properly to perform the agency contract. However, no further assumptions were considered to be necessary. Lord Hoffmann noted that a hypothetical purchaser would have paid fewer years' purchase for a declining agency than for one in an expanding market. It was therefore necessary to consider the circumstances as they existed in the real world at the time: what the earnings prospects of the agency were and what people would have been willing to pay for similar businesses at the time.

The French method of calculating compensation was rejected on three grounds. Firstly, it was considered that the function of the Commission's Report had been to consider the implementation of Article 17 and to propose any amendments considered necessary; not to indorse any particular method of calculation. Secondly, Lord Hoffmann highlighted that the French and English courts only differ in their method of calculating the damage suffered. Case law of the European Court of Justice has made it clear that the method of calculation is a matter for each Member State to decide. Thirdly, the market conditions that commercial agencies in France operate under was noted to be different to those prevailing in England.

In analysing the authorities, Lord Hoffmann was unconvinced by the reasoning of an Extra Division of the Court of Session in the case of *King v Tunnock*, stating that the goodwill in a business disappeared when it closed (in this case, the Extra Division of the Court of Session had awarded £27,144 compensation which was equal to the gross commission that the agent had earned in the two years before the business was closed).

Lord Hoffmann agreed with the judge in *Tigana Ltd v Decoro* that, in general, the value of the agency should be fixed by reference to its net earnings because that is what will concern the hypothetical purchaser. Nevertheless, those factors set out in paragraph 89 of the *Tigana* judgment, that had hitherto been regarded as the best test for assessing compensation, were of limited value, given the lack of any indication of the weight to be attributed to each factor.

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<sup>4</sup> COM(96) 364 final

Lord Hoffmann declined to interfere with the first instance award of £5,000, which had been approved of by the Court of Appeal. He added that in the circumstances, the judge could not have been faulted if he had simply dismissed the claim.

The three additional comments that Lord Hoffmann made are worthy of further analysis. Firstly, it had been argued on behalf of Mr Lonsdale that a principle should not be adopted which required valuation evidence on the grounds of the significant cost involved when compared to the amounts at stake in most claims. The Court of Appeal had considered that in most cases an expert witness would be of use to the court but that in some instances, it might be sufficient to provide the judge with all the relevant information to enable him to act as a valuer. Lord Hoffmann however was of the view that in future, very few cases will go to court, once it is appreciated that compensation is for the loss of the value of the agency. The parties should be able to agree on an appropriate valuation, with the benefit of advice about the going rate for such businesses. Nevertheless, when matters do reach court, it is essential that the judge is provided with some information about the standard methodology for the valuation of such businesses.

Secondly, the Winemakers' Federation of Australia Inc, who were given leave to intervene, were concerned about a situation where the agent is able to transfer the goodwill he has created with customers to another principal. Lord Hoffmann considered that the answer lay in the process of valuation: if in reality the hypothetical purchaser would be in competition with the former agent and it appeared that all the customers were likely to defect to the former agent, he would be unlikely to pay much for the agency.

Thirdly, in relation to the question of whether a reference should be made to the European Court of Justice, this was unnecessary. The wording of the Directive was clear as to what the agent should be compensated for. The method of valuation had been left to the domestic laws of the Member States and therefore it was for the House of Lords to resolve any existing uncertainty and not the European Court of Justice.

### **Commentary**

It remains to be seen whether there will be a down-turn in the number of cases going to court because parties have managed to agree on an appropriate valuation. What is certainly clear is that when cases do reach the courts, expert evidence will be required, at the very least, to enable the judge to ascertain the standard methodology for the valuation process. It is hoped that with time, the court will build up sufficient experience to be able to assess compensation in standard cases, without recourse to expert evidence.

The decision of the House of Lords has left agents vulnerable to being left with little or no compensation where principals elect to close their business. By contrast, those agents in highly successful agencies stand to receive significantly more than they may hitherto have expected to receive.

*The Claimant in Lonsdale was represented by Philip Moser.*

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