

WORKING WITHOUT A CONTRACT

...WILL I EVER GET PAID?

EDITORIAL | GERALD M. NEWMAN AND DAN BEEDERMAN

Reps often provide their valuable professional services without the benefit of a formal written contract, or even a less formal, but equally enforceable, oral contract.

In such situations, the rep is often told by the principal that they are not going to be paid despite the fact that the rep has just brought in significant business. The principal contends that the sale was “outside” of an existing contract, or that no contract exists between the parties. Typically, with a great deal of resignation, the rep wonders whether or not they will ever be paid. But alas, all is not lost. As we discuss in this article, the absence of a contract does not *necessarily* mean that a rep will not be able to recover reasonable compensation for their successful sales efforts.



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How Does This Problem Occur?

There are any number of reasons how it can happen that a rep performs its services without a contract — almost all of which are entirely preventable. Many times a rep is so thrilled about getting a new line that it utterly disregards the fact that the term of the proposed rep agreement is for a set period of time — such as for one year — but without an automatic renewal or “evergreen” provision. Instead, the agreement requires that the rep and principal enter into written extensions on a year-to-year basis, or even an entirely new contract. Often, the first time that a rep realizes there is a problem is when it finds a long-expired agreement at the bottom of a dusty file drawer, exactly where it was placed years earlier — having not seen the light of day or been reviewed since it was signed.

The same dilemma occurs when a rep continues to provide its services after both its contract and its principals have “expired.” It is not uncommon for a rep to learn suddenly that one of its long-time principals has been acquired by another company. Not wanting to rock the boat, the rep dutifully continues to call on customers in its territory as if nothing has changed — holding its breath until it learns its fate. If ultimately it is terminated, what happens to all of the orders and business that came in before the principal was acquired? Will the rep be paid for orders that came in thereafter? If so, on what basis?

Another variation on this theme occurs when the rep’s efforts result in sales that are not commissionable under the express terms of an existing rep agreement, either because the products are not of the type included in the rep agreement, or because the customer is not located in the rep’s assigned territory. Two such cases are illustrative of these two types of situations. One involved a rep who was approached by one of its principals to sell a newly developed product line that did not exist at the time that the rep agreement was signed. The rep was assured that it would be receiving either a new contract or an addendum to its existing contract that would cover the new product line. Before that could happen, the rep brought in a huge, long-term design-in order — thereby causing the principal to decide that it no longer needed the rep’s services for that purpose, or to pay the rep for what it had accomplished in such a short time — mistakenly believing that the new product line “sells itself.”

The second instance, which unfortunately is becoming more prevalent today as a result of the reduction of our manufacturing base, occurred when a customer in a rep’s territory decided not to buy a component part directly from the rep’s principal. Instead, the customer ordered a finished product from an off-shore OEM, which, per the customer’s specifications, purchased and incorporated the principal’s components into its own products, which the OEM then sold to the rep’s customer. Hence, the principal’s actual customer in this instance was the overseas OEM, which took delivery of and used the principal’s products. Unfortunately for the rep, the OEM was not in its territory and its principal refused to pay a commission — even though the rep and the rep’s customer were responsible for the sale itself.

How to Avoid the Problem

Before discussing how to possibly turn a sow’s ear into a silk purse, it is important to recognize these types of scenarios and to take the necessary steps to avoid them, or at least to minimize their impact on your business.

In the first example, the problem could have been avoided had the rep read the contract and been aware of its terms and inherent limitations. If at all possible, avoid a contract for a set term, unless it also includes an “evergreen” provision (where permitted by law), through which the agreement will automatically renew for successive terms, absent some affirmative step to terminate it. Moreover, don’t just file your rep agreements away in a drawer and forget about them. Make sure to diary any important dates (a perfect use for your PDA) and perform an annual audit of all of your rep agreements. Don’t be caught short because you either didn’t read the contract or remember its terms.

The second scenario is more problematic because a rep typically is not consulted by a principal prior to the sale of its company. Again, a well-drafted rep agreement will try to cover the situation by providing a mechanism for recovery of commissions for all orders and business opportunities that were generated prior to the sale of the principal’s business — obligating the principal to assure that the rep will be paid for such orders, either by the principal itself or by its successor. Also, not every “sale” of a company results in a change or termination of the pre-existing relationship between a principal and its representative. It typically does

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when the principal's assets are sold, but doesn't if there is a "stock deal," where the purchaser acquires the stock ownership of the principal. In that case, the new owner stands in the shoes of the prior owner, with the corporate entity itself continuing to operate as before, with the same pre-existing contractual obligations.

In the third scenario, the rep can't be so thrilled by the prospect of getting an order — either for the sale of a new product or to a customer outside of its territory — that it forgets the need to confirm that it will be paid for its services. Even if time or circumstances don't permit for the drafting and execution of a revised rep agreement, the rep should at least make sure to confirm its principal's agreement to pay a commission for such business. It is as easy as sending an email stating: "Thanks for the new opportunity with [the new product/in the new territory/with the new customer]. Please confirm via return email that all resulting sales will be commissionable under the terms of our existing sales representative agreement." If you don't get a prompt return email because the principal is too busy doing other things — be warned!

Will I Get Paid, and If So, How Much and On What Basis?

Now, after learning about how it can happen, and how to try to avoid it, does the rep have any legal recourse to recover unpaid commissions if it does happen? Well, if there truly is no contractual basis for a claim, or if a fraud claim is too difficult to prove (which it often is), is the rep out of luck? **The simple answer is, No!**

Under certain circumstances, a court still can award damages to remedy an inequitable situation, such as when someone knowingly receives the benefits of another's labors, without there being a contractual obligation to compensate that person. The technical name for this legal doctrine is *quantum meruit*, a Latin phrase which literally means "as much as he delivered." Often used interchangeably with terms like "unjust enrichment" and "implied contract at law" (although there are slight differences), the doctrine of quantum meruit allows a court to award just compensation for valuable services rendered for the benefit of another party, when the recipient who accepted the benefit either knew or reasonably should have known that the other party expected to be paid. In many cases, courts have utilized this doctrine to compensate sales reps who have been denied commissions for orders it procured.


In one such case, a sales representative, with its principal's knowledge and encouragement, solicited and procured orders from customers located outside of its assigned exclusive territory. However, the principal then refused to pay any commission because their written agreement provided that the rep would receive a commission only on orders that originated from customers in its territory. The court ultimately awarded commissions to the rep for the extra-territorial sales on the theory of quantum meruit, which, as the court indicated, implies a promise that a person will "pay a reasonable and just compensation for valuable services or materials provided at that person's request or with that person's approval." As the court further recognized, "Recovery is permitted under quantum meruit if it is proved that services were provided at the request or with the acquiescence of defendant (the principal), that those services had a certain reasonable value, and that defendant, despite demands of plaintiff (the rep) has failed and refused to pay the reasonable value of plaintiff's labor." To determine the value of those services, the court utilized the very terms of the parties' existing contract, finding it to be persuasive evidence as to the reasonable value of the representative's services.

A similar result occurred in another case where a rep continued to provide its services following the expiration of an initial six-month "trial contract." Under that contract the rep could not call upon and would not receive a commission for sales to a customer that was identified as being a "house account." Subsequent to the expiration of the six-month written contract, the rep continued to provide its services for four years without the benefit of a written or oral contract. During that time, with the principal's knowledge, the rep called upon and procured orders from the customer that the initial contract had identified as being a "house account." After the rep requested payment of commissions for such sales, it received a letter from its principal terminating "all written and/or verbal agreements" between them. However, because there was no express contract between the parties following the expiration of the initial trial contract, the court ruled that the rep was entitled to reasonable compensation for such sales on the theory of quantum meruit. Specifically, the court found that, "it was not reasonable for [the principal] to believe that the [representative] would perform months of services on the [customer account] in an effort to generate sales and not expect to be compensated. Recovery in quantum meruit is proper when it would result in unjust enrichment to the party for whom the services were performed."

Expert Witness Testimony

This is not to say that quantum meruit is available in all circumstances or that it is a perfect remedy, for it is not. In the absence of a prior contract between the parties establishing a reasonable basis for valuing the rep's services, a court likely will have to rely upon the testimony of expensive competing expert witnesses at the trial to determine the value of the rep's services and the resulting amount of damages to be awarded, if any. This can result in the representative being awarded damages at a far lesser rate than what it otherwise would have received under the terms of a freely negotiated contract. Perhaps more important from a strategic sense, it is likely that in the absence of a written contract, the representative may be denied a basis to recover statutory damages as provided in sales representative protection acts passed in many states.

Many of these acts would otherwise have permitted the rep to recover two or three times its actual damages, plus attorneys' fees. This is because remedies under most sales rep statutes are based on a claim for breach of a written or oral contract and not for recovery under quantum meruit, which remedy depends on the absence of a contract.

In the end, rather than relying on the possible application of the doctrine of quantum meruit, a rep would be better served to negotiate a sound contract, know its terms, review it on an annual basis and make sure that any deviation from the contract is properly memorialized. In so doing, it will stand a better chance of being fully compensated for the services it renders on behalf of its principal. 

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