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SUCCESSOR LIABILITY IN SALES REPRESENTATION AGREEMENTS ©

By Randall J. Gillary

A recent case in Michigan highlights one of the key considerations for manufacturers' representatives in their sales representation agreements. In *Zantel Marketing Agency v Whitesell Corporation,* 265 Mich App 559 (2005), the plaintiff sales representative prevailed in a jury trial, and obtained a total verdict in excess of $500,000. The judgment included sales commissions, penalty damages under the Michigan Sales Representative Commission Act, court costs, and attorney fees. Unfortunately, the Michigan Court of Appeals reversed the trial court and held that a directed verdict should have been entered against the plaintiff. The net effect of the Court of Appeals' decision was that the plaintiff sales representative lost the jury verdict of over $500,000 and came away with nothing.

Factual Background

Zantel Marketing Agency entered into a written sales representation agreement with Stamptech Manufacturing Company in 1997. The sales representation agreement granted Zantel the exclusive right to represent Stamptech in Canada and required Stamptech to pay Zantel sales commissions of 5%. Language was also included indicating that the agreement was

> "*not transferable to a third party* but will be honoured by new ownership, successors and assigns of either party and the terms and conditions can be mutually agreed upon with respect to the element of changes that might be considered."

Stamptech entered into an asset sale agreement with Whitesell Corporation in August of 1998. Pursuant to the asset sale agreement, Whitesell purchased only assets and no liabilities. In reversing the trial court's decision and the jury verdict for the plaintiff Zantel Marketing Agency, the Michigan Court of Appeals wrote:

> "Plaintiff argues alternatively that WOM's [Whitesell of Michigan] agreement to assume liability for the agency agreement should be implied, based on the conduct of Whitesell in writing commission checks to [Zantel's owner] Ali, the statements made to Ali by Whitaker, and the correspondence to Ali, Zantel and Stamptech clients that used the names
> Whitesell, WOM and Stamptech interchangeably. We disagree. *Under Michigan law, a corporation that acquires the assets of another corporation is not liable for the selling corporation's obligations, absent certain circumstances* (emphasis added) . . . Such circumstances exist where: (1) the transaction amounts to a consolidation or merger; (2) the acquiring corporation expressly or impliedly agrees to assume the selling corporation's obligations; (3) the new corporation is a mere continuation of the old

> corporation; or (4) the sale is fraudulent . . . Here, because WOM expressly limited its liabilities in the asset agreement, an implied agreement to assume any liability to Zantel arising from the agency agreement cannot be found . . ."

The net result was that Zantel procured a significant amount of business for Stamptech; Stamptech sold its assets (including purchase orders) to Whitesell; Whitesell retained all of the business; but Zantel received no sales commissions. This was obviously not a good outcome for Zantel, the sales representative.

A Common Problem

The problem with the sales representation agreement was that there was no contractual obligation created for the principal to include commission payment protection for the sales representative in the asset sale agreement. This is a potential problem area for any manufacturers' representative. In every sales representation agreement, manufacturers' representatives should consider commission protection in the event of a sale of assets a high priority item.

This is a common problem in Michigan, where the automotive industry is the driving force behind the state's economy. Asset sales, like the one in *Zantel*, occur on a regular basis. Anyone following the auto industry knows that the status of auto suppliers in the state of Michigan is in quite a state of flux. There have been several high profile automotive supplier bankruptcies. Acquisitions, mergers, and consolidations are happening at a fairly rapid pace. Unless there is proper planning at the time that the sales representation agreement is entered into, the outcome of *Zantel* is likely to happen to you.

It is important here to note that the typical "Successor and Assigns" language found in most sales representation agreements is not sufficient. An asset purchaser is generally not considered to be a successor or assignee. The typical asset purchase agreement assumes an express exclusion upon the assumption of any liabilities not specifically identified in the agreement. Generally the first liability to go by the wayside is the commission liability to the sales representative of the asset seller.

The net result of this is that, regardless of the good intentions of your principal at the time of the signing of your sales representation agreement, if your principal does not place upon the asset purchaser the obligation to pay your commissions, then you may be out of luck. When it comes to cashing out his business, your principal is deciding whether money is to go into his pocket or your pocket. It does not take a rocket scientist to figure out who is going to come out on the short end of that stick. The trick is to put the burden on the principal to protect you at the time that the sales representation is signed in the first place and before you have procured any business. After the business is in the door and the principal is cashing out, it is too late. Neither your principal nor the asset purchaser has any incentive to protect your commissions for you.

This particular problem is addressed in my book, *Protecting Your Commissions—A Sales Representative's Guide*. In Chapter 2, "Important Considerations in Written Sales Representation Agreements," in the section entitled "Successor Liability" beginning on page 52, I discuss my solution to this problem. I recommend that manufacturers' representatives include a specific provision in their sales representation agreements that addresses what will happen in the event of a sale of the assets or business of the principal. Such a provision should specify that, in that event, the agreement will be binding upon the purchaser to the same extent as it would be binding upon the original principal if no transfer of the assets or business had taken place. The provision should also require the principal to notify the asset purchaser of the continuing commission obligation. The agreement should also include language which provides that, in the event the asset purchaser does not pay the commissions, the original principal will be obligated to pay the commissions, unless the purchaser specifically assumes the commission obligation in writing. My suggested language appears on pages 54-55 of the book. I recently added the provision allowing the principal to avoid the commission payment obligation if the asset purchaser specifically agrees in writing to pay the sales representative's commissions.

I would note that this language has never actually been tested in court. I believe that it is vitally important, however, for a sales representation agreement to specifically address the issue regarding the manner in which commissions will be treated in the event the principal sells the assets or any commissionable business. The problem with most sales representation agreements is that the trigger for the payment of commissions is the manufacture and sale of a part by a principal. Once the principal transfers the assets and is no longer making and shipping parts, there is no trigger for the payment of commissions. This is not to say that an effective theory of recovery cannot be formulated if the issue is not addressed in the sales representation agreement. A creative attorney can often obtain a good result as long as there is not an express provision in the sales representation agreement precluding commissions in the event of an asset sale. You are definitely better off, however, if you include protection in your sales representation agreement to cover an asset sale by your principal.

The practical problem created by language protecting the manufacturers' representative's commissions in the event of an asset sale is that it negatively affects the marketability of the principal's assets and business. You will likely find most principals reluctant to include this language in the sales representation agreement. My view, however, is that your principal should never be allowed to sell the business which the manufacturers' representative procured for the principal without fair compensation. Your principal should not be able to cash out the business you brought in without fairly compensating for your efforts. It is extremely important that protection for the manufacturers' representative in the event of the sale of the assets, including transfer of purchase orders, should be included and should be treated like any other termination.

I have one client who, after reading my book, decided this issue was important enough for him to renegotiate a 36-year-old sales representation agreement. The 1969 contract even had a provision requiring life-of-part commissions for all production business. My client was willing to give some commission relief in exchange for commission protection in the event of a sale or transfer of the assets or business.

If you are in the process of negotiating a new sales representation agreement, I strongly recommend that you include a provision specifically addressing the manner in which commissions will be treated in the event of a sale or transfer of any of the principal's assets or of any commissionable business. I also strongly recommend that you consider revisiting any of your current sales representation agreements to see if it would be appropriate to raise this issue with your current principals. This may be quite difficult to do with an existing contract, but if you think creatively, you may be able to fashion an equitable result which is beneficial to both sides. If nothing else, this is a good comeback to your principal when they are putting pressure on you to reduce commissions. I guarantee that you do not want to be in a situation in which you have spent many years establishing new business for your principal only to find that your principal has decided to sell its business, leaving you with the possibility of receiving nothing for your efforts. If you do not adequately plan for this contingency, you may be sorely disappointed if an asset sale takes place.

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About the Author

Randall J. Gillary is recognized as a top legal expert on sales commissions. He has handled landmark sales commission cases and is an active litigator, counselor, legal writer, and lecturer. His law practice is devoted to insuring that sales professionals are paid the commissions they have earned. He is also the author of *Protecting Your Commissions—A Sales Representative's Guide*. To contact Mr. Gillary or to order a copy of his book, you may visit his website at www.gillarylaw.com, call 1-800-801-0015, go to Amazon.com, or contact him at The Law Offices of Randall J. Gillary, P.C., 201 W. Big Beaver Road, Ste. 1020, Troy, MI 48084.