B2/2005/1174, Neutral Citation Number: [2006] EWCA Civ 63

IN THE SUPREME COURT OF JUDICATURE
IN THE COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE OXFORD COUNTY COURT
HIS HONOUR JUDGE CHARLES HARRIS QC
4OX03380

Royal Courts of Justice
Strand, London, WC2A 2LL

Wednesday 8th February, 2006

B e f o r e:

LORD JUSTICE JACOB
LORD JUSTICE MOORE−BICK
AND
LADY JUSTICE HALLETT

− − − − − − −

GRAHAM LONSDALE

Claimant

− v −

HOWARD & HALLAM LIMITED

Defendant

− − − − − − − − −

(Transcript of the Handed Down Judgment of
Smith Bernal WordWave Limited
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Tel No: 020 7421 4040 Fax No: 020 7831 8838
Official Shorthand Writers to the Court)

Mr. Philip Moser (instructed by Morgan Cole) for the claimant
Mr. Oliver Segal (instructed by Harvey Ingram LLP) for the defendant

J U D G M E N T

Lord Justice Moore−Bick:

1. This appeal raises some important questions relating to the application of The Commercial Agents (Council Directive) Regulations 1993 by which Council Directive 86/653/EEC was implemented in Great Britain. The Regulations govern the relations between commercial agents and their principals in relation to activities carried on within England and Wales and Scotland. Among other things they deal with the formation and termination of a relationship of this kind, the rights and obligations of the agent and principal to each other, the agent's remuneration and his right to receive what the Regulations describe as an indemnity or compensation on the termination of the relationship.

2. A commercial agent is defined in Regulation 2(1) as

> "a self−employed intermediary who has continuing authority to negotiate the sale or purchase of goods on behalf of another person ("the principal"), or to negotiate and conclude the sale or purchase of goods on behalf of and in the name of that principal."

3. The claimant in this case, Mr. Graham Lonsdale, was a commercial agent for the defendant, Howard & Hallam Ltd, a shoe manufacturing company, selling its products to shoe shops in the South East. His agency began on 1st January 1990 and continued until 30th June 2003 when it was terminated after a period of notice as a result of the closure of Howard & Hallam's business due to rising costs and falling sales. No complaint was made about the termination of the agency and no suggestion was made that Mr. Lonsdale had a claim for compensation of any kind other than that which arises under the Regulations themselves. It was accepted that the Regulations gave him a right to compensation, but the parties could not agree on the amount to which he was entitled. Howard & Hallam paid Mr. Lonsdale £7,500, but he did not think that represented the full amount to which he was entitled and eventually he began proceedings in the Oxford County Court seeking £19,670, an amount that was roughly equal to two years' gross commission calculated by reference to the average of the last five years of his agency less the amount he had already received.

4. Before the judge Mr. Moser, who appeared on behalf of Mr. Lonsdale, submitted that, where the agency had persisted over a reasonable period of time and the agent had performed his functions competently throughout that period, he should as a

general rule receive by way of compensation under regulation 17(6) an amount equal to two years' gross commission. He did not go so far as to submit that that was an established rule of practice, but he did submit that it was a clear guideline which had been applied in the past and ought to be followed in cases of this kind. In support of that argument he drew the judge's attention to the approach adopted by the French courts in such cases and to previous decisions of courts in this country and Scotland. Mr. Segal for Howard & Hallam submitted that there was no such guideline, that if commission were to be taken as the basis for assessing compensation it should be the amount received by the agent after deducting expenses and that the payment already made to Mr. Lonsdale was as much as he was entitled to receive.

5. Regulation 17 provides as follows:

> "**17 Entitlement of commercial agent to indemnity or compensation on termination of agency contract**
>
> (1) This regulation has effect for the purpose of ensuring that the commercial agent is, after termination of the agency contract, indemnified in accordance with paragraphs (3) to (5) below or compensated for damage in accordance with paragraphs (6) and (7) below.
>
> (2) Except where the agency contract otherwise provides, the commercial agent shall be entitled to be compensated rather than indemnified.
>
> (3) Subject to paragraph (9) and to regulation 18 below, the commercial agent shall be entitled to an indemnity if and to the extent that-
>
> (a) he has brought the principal new customers or has significantly increased the volume of business with existing customers and the principal continues to derive substantial benefits from the business with such customers; and
>
> (b) the payment of this indemnity is equitable having regard to all the circumstances and, in particular, the commission lost by the commercial agent on the business transacted with such customers.
>
> (4) The amount of the indemnity shall not exceed a figure equivalent to an indemnity for one year calculated from the commercial agent's average annual remuneration over the preceding five years and if the contract goes back less than five years the indemnity shall be calculated on the average for the period in question.
>
> (5) The grant of an indemnity as mentioned above shall not prevent the commercial agent from seeking damages.

(6) Subject to paragraph (9) and to regulation 18 below, the commercial agent shall be entitled to compensation for the damage he suffers as a result of the termination of his relations with his principal.

(7) For the purpose of these Regulations such damage shall be deemed to occur particularly when the termination takes place in either or both of the following circumstances, namely circumstances which-

(a) deprive the commercial agent of the commission which proper performance of the agency contract would have procured for him whilst providing his principal with substantial benefits linked to the activities of the commercial agent; or

(b) have not enabled the commercial agent to amortize the costs and expenses that he had incurred in the performance of the agency contract on the advice of his principal.

(8) Entitlement to the indemnity or compensation for damage as provided for under paragraphs (2) to (7) above shall also arise where the agency contract is terminated as a result of the death of the commercial agent."

6. Regulation 18 describes certain circumstances in which an agent is not entitled to payment of the indemnity or compensation provided for in regulation 17. It provides as follows:

"**18 Grounds for excluding payment of indemnity or compensation under regulation 17**

The indemnity or compensation referred to in regulation 17 above shall not be payable to the commercial agent where-

(a) the principal has terminated the agency contract because of default attributable to the commercial agent which would justify immediate termination of the agency contract pursuant to regulation 16 above; or

(b) the commercial agent has himself terminated the agency contract, unless such termination is justified-

(i) by circumstances attributable to the principal, or

(ii) on grounds of the age, infirmity or illness of the commercial agent in consequence of which he cannot reasonably be required to continue his activities; or

> (c) the commercial agent, with the agreement of his principal, assigns his rights and duties under the agency contract to another person."

7. As the judge pointed out, the Regulations themselves give no explicit guidance as to the amount of compensation which the agent is entitled to receive. Having referred to the decision of the Inner House of the Court of Session in *King v T. Tunnock Ltd* [2000] ScotCS 70, [2000] Eu.L.R. 531, the decision of Morland J. in *Ingmar GB Ltd v Eaton Leonard Technologies Inc.* [2001] EWHC QB 3, [2001] Eu.L.R. 755 and the decision of Davis J. in *Tigana Ltd v Decoro Ltd* [2003] EWHC QB 23, [2003] Eu.L.R. 189, he concluded that Mr. Lonsdale was entitled to be compensated for the value of the agency of which he had been deprived. He declined to take account of the approach adopted in other jurisdictions and held that on the facts of this case Mr. Lonsdale was entitled to no more than £5,000.

8. The judge's approach was to seek to identify from the language of the Regulations themselves and the decided cases the nature of the damage suffered by the agent in respect of which he is entitled to be compensated before attempting to place a monetary value on it. In my view that was a sensible approach to take, but it is convenient to begin by considering a number of previously decided cases in which the assessment of compensation has been considered.

9. The first case to which we were referred was *Page v Combined Shipping and Trading Co Ltd* [1997] 3 All E.R. 656. The agent in that case, Mr. Page, had been engaged to trade in commodities on behalf of the defendant for a minimum period of four years. Six months after the agreement had been signed the defendant informed him that its parent company abroad had decided to close down its trading activities. Mr. Page began proceedings claiming compensation under regulation 17 and applied for an injunction to prevent the defendant from moving its assets abroad. The judge dismissed the application on the grounds that, since the defendant could have operated the agreement for the remainder of its term in a way that would not have enabled him to make any money, he did not have an arguable case that he was entitled to recover a significant sum by way of damages. This court reversed the judge's decision, holding that it was arguable that Mr. Page was entitled to recover compensation under regulation 17(7) calculated by reference to the amount of commission he would have earned if the contract had been performed in accordance with the parties' original intention. The decision is of interest mainly for the dictum of Staughton L.J. at page 660f that

> "commercial agents are a down−trodden race and need and should be afforded protection against their principals",

which has been much relied on in subsequent cases, and for his observation at page 660g that the preamble to the Directive

> "points fairly strongly to an intention to depart from the domestic legal provisions of the various countries in the

> Community, or at any rate some of them, and achieve a regime which is new to some and will be the same for all."

As one can see from the earlier passage in his judgment at page 658j−659a, this latter comment was intended to emphasise the fact that it was at least arguable that the Directive and the Regulations provided a remedy that was not available at common law. However, since it was sufficient for the court to decide that Mr. Page had an arguable case, the decision is ultimately of limited assistance.

10. The questions at the heart of the present case are whether there is, or should be, a general rule that in the ordinary case compensation should be assessed at two years' gross commission, and if not, on what basis it should be assessed. What may for convenience be called the "two years' commission" rule has been derived from the practice of the French courts as described in the report into the working of the Directive published by the European Commission in July 1996 pursuant to Article 17.6. The report is of assistance inasmuch as it describes the background to the Directive, which is to be found in the existence of two rather different approaches to the compensation of commercial agents following the termination of their agency agreements, the indemnity system and the compensation system, and explains that it represented a compromise between Member States which had already adopted one or other approach. The indemnity approach is said to have been modelled on the German Commercial Code; the compensation approach is said to have been based on French law. The Commission noted that "by judicial custom" the level of compensation in France was fixed at two years' gross commission, subject to adjustment in the light of the particular circumstances of the case. According to the report, the French courts have justified the payment of compensation on the ground that it represents the cost to a successor of purchasing the agency business or on the ground that it represents the time it takes for the agent to reconstitute the client base of which he has been deprived. In relation to the operation of the compensation system the report noted that in the United Kingdom parties were attempting to apply common law principles that are directly opposed to the well−established method of calculating compensation in France by taking account of developments after the termination of the contract and so introducing the concept of mitigation. Having referred to the French practice of awarding two years' commission, the report noted that in the United Kingdom there was no real concept of goodwill attaching to an agency which the agent had a right to share.

11. The Commission's report provided the basis for much of the discussion in *King v Tunnock* in which the Inner House of the Court of Session considered the nature of the agent's right to compensation and the basis on which that compensation should be assessed. In that case the claimant was employed as a commercial agent by the defendant which carried on business as, among other things, a baker. The claimant's business consisted solely of selling the defendant's cakes and biscuits. The relationship between the parties came to an end when the defendant decided to close its bakery business. The claimant brought proceedings claiming compensation under regulation 17(6) which, he submitted, was to be assessed by reference to the value of the agency at the date of termination rather than on the basis of any future economic loss. He argued that compensation should be assessed without regard to events

occurring after the date of termination and that when assessing the amount of compensation to which he was entitled the court should follow the established practice of the French courts in awarding two years' gross commission.

12. Having concluded that the agent was entitled to receive compensation for the loss of his business, the court turned its attention in paragraphs 49−51 of the judgment to the assessment of compensation. It noted that even in France the two years' commission rule is only a benchmark and went on to examine the particular circumstances of the case. It appears to have accepted that earning potential was an important factor in valuing an agency and recognised that there might be cases in which it would be necessary to adduce evidence of the valuation of agencies in the particular local market. There was no such evidence in that case, however, and indeed the court commented on the limited amount of evidence before it of the value of the business to the claimant. However, having regard to the duration and previous profitability of the agency it concluded that the claimant would have expected to receive a capital sum equal to at least two years' earnings in order to give it up and held that an award of that amount would not be unreasonable. I do not think it would be fair to say that the court adopted the French rule as such, even as a general guideline, although it did in my view derive considerable support for its ultimate decision from it and may to that extent be said to have encouraged its adoption by others.

13. The next case drawn to our attention in which the issue was discussed was *Duffen v Frabo S.p.A.* [2000] Eu.L.R. 167 in which an agency agreement was terminated some eighteen months before it would have expired naturally. His Honour Judge Hallgarten Q.C. declined to accept that the court should follow the French practice and apply the two years' commission rule as a matter of routine. Having considered the terms of regulation 17(7) he concluded that the right approach in that case was to look at the net earnings that the agent might have made during the remainder of the period for which his agency would have run had it not been terminated prematurely, but without taking into account common law concepts such as avoided loss and mitigation. He considered that it would have been offensive in that case to base his award on gross rather than net earnings since that would have given the agent an undeserved windfall. The judge's approach, therefore, was to award compensation for loss of future earnings, ignoring the ordinary rules of mitigation.

14. The question next arose for consideration in *Ingmar GB Ltd v Eaton Leonard Inc.* In that case Morland J. considered himself bound by the decision of the Court of Session in *King v Tunnock* which he understood as adopting the two years' commission rule as a general guideline. (As I have already indicated, I do not think the court went as far as that, although it did give some support to the adoption of that approach.) However, he concluded that to apply that rule in the case before him would result in injustice to the defendants and an excessive windfall for the claimants. He therefore considered it appropriate to depart from the guideline as he understood it to be.

15. In *Tigana v Decoro* the court again considered at length the proper approach to the assessment of compensation. In paragraphs 87 and 88 of his judgment Davis J. began by setting out a number of matters on which the parties were agreed. They included

the proposition that common law principles of mitigation and avoidable loss have no part to play in the assessment of compensation, because, as counsel had put it, "the focus is on the position at the time of termination: one looks back, not forward" and also the proposition that the court ought to adopt a broad brush approach. The judge himself pointed out, however, that the court could not simply alight on a figure by reference to its "feel" of the particular case. There had to be some method to the assessment, even if the approach were broad.

16. In paragraph 89 the judge set out a list of factors, fourteen in all, which he suggested were likely to require consideration when assessing compensation, recognising that the list could not be exhaustive and that some of the factors might not feature at all in some cases. It will be necessary to return to these at a later stage in this judgment. Then in paragraph 90 he said this:

> "It is clear that the "damage" suffered by a commercial agent as a result of the termination of the agency (Regulation 17 (6)) is - generally speaking (and breach of contract cases aside) − to be regarded as a putative loss and not simply (by common law standards) actual loss. This is shown by the exclusion of principles of mitigation and applicability of the compensation provisions to termination on death or retirement. Clearly one important element, as the recitals to the Directive show, is to avoid a principal being unjustly enriched by retaining for itself without payment the entirety of the benefit of goodwill to which the activities of the agent during the agency have contributed. But another element (which finds both reflection and emphasis in Regulation 17(7) (a)) is to compensate the agent for the loss of a beneficial agency contract. One can perhaps there see some analogy with redundancy payments in an employment context: although the analogy cannot be pushed too far, since the policy considerations behind redundancy payments for employees are rather different."

17. Davis J. then considered at some length the decision in *King v Tunnock* and the summary of French law and practice in the Commission report. He was not attracted by the suggestion that the courts of this country should adopt the French practice, partly because, as he understood it, the Directive itself left it to each Member State to work out the method of assessment for itself and partly because he did not think that a benchmark of that kind could properly reflect the wide range of circumstances in which compensation would have to be assessed. In the event, after taking into account the factors to which he had referred in paragraph 89 and what he called the "balance sheet" of the particular factors relied on by each side, the judge assessed compensation by reference to the claimant's net earnings during the whole of the 14−month period of its activities on behalf of the defendant. As far as I can see, he arrived at that decision on the basis that it provided proper compensation in all the circumstances of the case and because he was satisfied that it produced an award that was fair and proportionate.

18. In *Cooper, Watkins and Bartle v Pure Fishing (UK) Ltd* [2004] Eu.L.R. 664 the claimants were commercial agents for the sale of fishing tackle manufactured by the defendants. In each case their contracts were expressed to run for a period of six months, but had been renewed for successive periods of six months each time they expired. In June 1999 two weeks before their current contracts expired the defendant gave notice to the claimants that they would not be renewed. The contracts therefore came to an end in accordance with their terms. His Honour Judge Kershaw Q.C. held that in those circumstances the claimants were entitled to receive compensation under regulation 17(6) and his decision was affirmed by this court on appeal (see [2004] EWCA Civ 375).

19. When the judge came to assess compensation he was persuaded by the decision of Morland J. in *Ingmar GB Ltd v Eaton Leonard Technologies Inc.* that he should adopt the guideline of two years' commission as had been discussed in *King v Tunnock* . Having found that goodwill is an important part of the value of an agency, he reached the conclusion that it would be right to award compensation based on two years' receipts, but he did not give any further explanation of his reasons for doing so. That part of his decision was not challenged on appeal so the court was not asked to, and did not, express any view about it.

20. Finally it is necessary to refer to *PJ Pipe & Valve Co. Ltd v Audco India Ltd* [2005] EWHC 1904(QB). The claimant in that case was an agent operating in the petrochemical industry promoting and selling a variety of products, particularly valves. The defendant was a manufacturer of valves used in petrochemical processing plants. The claimant was engaged to act for the defendant under two agency agreements, one relating solely to products to be supplied to a particular petro−chemical complex in Nanhai, the other being a general agency agreement under which the claimant was given exclusive rights to represent the defendant and other suppliers for a period of two years. The latter agreement was terminated as far as the defendant was concerned as a result of the defendant's repudiation of it about twelve months before it was due to expire. As a result the agent brought proceedings claiming commission or damages in respect of orders placed with the defendant for equipment required for three different phases of a construction project at Bonny Island, Nigeria and compensation under Regulation 17.

21. Fulford J. found that the claimant had been the effective cause of the defendant's obtaining orders for equipment required for all three phases of the project at Bonny Island and he therefore held that it had earned commission in respect of all that equipment. It therefore became unnecessary for him to consider the alternative claim for damages which was apparently limited to the amount of commission which the claimant said it would have earned in relation to the equipment ordered for that project. There remained, however, the claim for compensation.

22. The first question the judge had to decide was whether the claimant was a commercial agent within the meaning of regulation 2(1) despite the fact that it did not have authority to agree commercial terms or prices on behalf of the defendant. He held that it was. That question does not arise for decision in this case and it is

therefore unnecessary for me to express a view about it. The judge then turned in paragraph 156 to the assessment of compensation. He noted that in this country the approach adopted by different courts has not been entirely consistent, referring to *King v Tunnock* , *Duffen v Frabo* and *Tigana v Decoro* , and he agreed with Davis J. that it was necessary to have regard to all the circumstances of the case while recognising the need to make a decision on a principled, logical and just basis (paragraph 162). He therefore rejected the claimant's submission that he should adopt the French approach of awarding two years' commission in favour of seeking to ascertain what the claimant had lost as a result of the premature termination of the agency. He found that the claimant would have effected one further successful introduction during the remaining twelve months of the contract, the value of which he assessed by reference to the average gross commission earned by the claimant from the six previous projects it had obtained for the defendant. In effect, therefore, the judge approached the assessment of compensation in broadly the same way as one would approach the assessment of damages for breach of contract.

23. One thing that emerges from these decisions is that there is no clear agreement on the principles governing the assessment of compensation under regulation 17(6). In most cases the courts have had regard primarily to the nature and duration of the agency and the commission the agent was able to generate from it as providing the basis for the assessment, but in *Duffen v Frabo* and *PJ Pipe v Audco India* the court looked primarily to future earnings as the basis of assessing compensation. It has been generally accepted (though the basis for it is not entirely clear) that the common law concept of mitigation has no part to play in the exercise, so that the court is not concerned with any steps that the agent might have taken to obtain other employment following the termination of the agency, and that a broad approach is to be adopted to the assessment of compensation. However, in none of the reported cases other than *Duffen v Frabo* is it at all easy to discern the basis on which the court reached its decision, other than by taking a figure which it considered fairly reflected all the various circumstances of the particular case. In *Tigana v Decoro* Davis J. recognised that the assessment of compensation ought to be undertaken in accordance with some organised method, but apart from identifying a large number of factors that he suggested should ordinarily be taken into account, it is not clear what method he actually adopted other than to make an overall assessment of what he considered to be fair in all the circumstances. The two years' commission rule derived from the practice of the French courts, which was given some prominence in *King v Tunnock* and appears to have influenced the court's decision in that case, has inevitably formed part of the discussion but has been widely regarded as unsatisfactory and has rarely been applied. In general, judges seem to have proceeded on the footing that regulation 17(6) requires them to make an award of compensation that is just and equitable in all the circumstances, rather than an award that compensates the agent for any specific loss he has suffered.

24. As has been observed in several cases, neither the Directive nor the Regulations deal expressly with the manner in which compensation is to be assessed. I do not find that surprising, however, since legislation providing a remedy of this kind usually describes the loss or damage in respect of which there is a right to compensation leaving it to the courts to assess the amount of compensation in accordance with established principles. In my view the main reason for the differences of approach to

the assessment of compensation one finds in the decided cases lies in a failure to apply the language of the Directive and the Regulations and to identify clearly the damage in respect of which the agent is entitled to receive compensation. It is, of course, well established that the Regulations must be construed in a way that gives effect to the Directive: see *Litster v Forth Dry Dock & Engineering Co. Ltd* [1990] 1 A.C. 546. In this case, however, the legislative technique adopted for the implementation of the Directive was to reproduce the English language text in a statutory instrument. Apart, therefore, from some restructuring of individual articles, some linguistic changes required to conform to established practices of Parliamentary drafting and some inevitable alterations reflecting the transition from a Council Directive to national legislation, the text of the statutory instrument reproduces in largely the same words the English language text of the Directive. As a result one gets little or no additional assistance from the language of the Directive itself when approaching the construction of the Regulations and there is no decision of the European Court which bears directly on the question. The problem, such as it is, lies in identifying the correct meaning of the Directive and the Regulations.

25. If there are decisions of courts of other Member States (principally in this case France) which shed light on this question, they might well be of assistance in reaching a correct conclusion, but they would not be binding on us and in any event none has been drawn to our attention. In this context I cannot help thinking that the Commission's report has been given too much weight in the discussion. It is no doubt helpful and informative to know how the French courts have applied Article 17 of the Directive, but the knowledge that the compensation system was based on the law previously in force in France has tended to lead judges in this country to assume that the Directive must be understood and applied in the way that it is understood applied in France, instead of approaching it as a piece of Community legislation in its own right. One consequence is that there has in my view been too great a readiness to assume that the common law approach must be rejected in all its manifestations in favour of a different approach which the Directive itself does not define. As a result there does not appear to have been a consistent attempt to identify the nature of the judge's task in assessing compensation or to determine exactly what paragraph (6) means when it refers to "the damage [the agent] suffers as a result of the termination of his relations with his principal". In order to perform that task it is necessary examine more closely the terms of Regulations 17 and 18.

26. The objectives of the Directive as they emerge from the preamble are the greater harmonisation of national laws relating to commercial agents with a view to promoting the single market and the enhancement of the protection available to commercial agents and the security of commercial transactions. However, the Council did not set out to achieve complete harmonisation between the laws of the different Member States in this area because it allowed them to choose whether the agent should be entitled to an indemnity or compensation on the termination of the agency. Thus Article 17.1 of the Directive provides as follows:

> "Member States shall take the measures necessary to ensure that the commercial agent is, after termination of the agency contract, indemnified in accordance with paragraph 2 or compensated for damage in accordance with paragraph 3."

27. It is convenient to begin the discussion by considering the concept of compensation. Article 17.3 of the Directive and regulation 17(6) provide that the agent shall be entitled to compensation for the damage he suffers as a result of the termination of his relationship with his principal. On the face of it, therefore, they give the agent a right receive compensation for any damage he has suffered; they do not simply provide for him to receive payment of an amount that is fair and reasonable having regard to all the circumstances of the case. This can be compared with the position which applies in relation to an indemnity. In that case Article 17.2 of the Directive and regulation 17(3) specifically provide that the agent shall be entitled to an indemnity, limited in amount, if and to the extent that the payment is equitable having regard to all the circumstances of the case. No comparable provision is made in relation to payment of compensation, however, from which I think one can fairly conclude that the intention was to provide full compensation to the agent for any damage that he has actually suffered rather than a right to receive a payment that is fair and reasonable having regard to all the circumstances of the case. The distinction is important because it goes to the heart of the task which the court is required to undertake when it has to assess how much the agent is entitled to receive by way of compensation in any given case.

28. To an English lawyer the expression "the damage he suffers as a result of the termination of his relations with his principal" is redolent of the language of breach of duty, but reference to other parts of the Regulations makes it clear that regulation 17(6) must have been intended to extend beyond the situation in which the agency is terminated by an unlawful act on the part of the principal. For example, paragraph (8) expressly provides for the payment of compensation in cases where the agency is terminated by the death of the agent and the effect of regulation 18(b) is that the agent's entitlement to compensation is not excluded in cases where he has terminated the agency himself on the grounds of age, infirmity or illness which prevents him from continuing his activities. This makes it necessary to ask what damage (using that word in its widest sense) the agent can be said to have suffered in those circumstances. One answer to the question is that he has suffered a loss of the goodwill attaching to the agency business that he would have enjoyed if his relationship with the principal had not come to an end. These provisions therefore support the conclusion that the purpose of the regulation is not to provide compensation for damage caused by a breach of duty (for which a claim could be made outside the terms of the Regulations in any event), but to provide compensation for the loss of goodwill for which a claim would not otherwise arise. In my view that conclusion is consistent with paragraph (7), both limbs of which contemplate that the agency has built up a fund of goodwill which, in the situation described in subparagraph (i), will enable the principal to benefit from it through profits generated in the future or which, in the situation described in subparagraph (ii), could have been expected to enable the agent to generate enough commission to amortize certain costs incurred in setting up the business. It is reinforced by regulation 18(c) which deprives the agent of any right to compensation if he transfers the agency to another person. In such a case it is reasonable to assume that he will have recovered any value attaching to the business as part of any payment he receives for the transfer. This view is also consistent with the description in the Commission's report of the philosophy which underlies the French law from which the Directive was apparently derived.

29. However, I do not think that it would be right to regard the loss of goodwill as the only damage in respect of which the agent may be entitled to receive compensation. Under paragraph (7)(a) the agent is deemed to suffer damage, and must therefore be entitled to recover compensation, when the agency is terminated in circumstances which deprive him of the commission which proper performance of the contract would have enabled him to earn while providing the principal with substantial benefits as a result of his activities. In such a case the value of the business at the date of termination ought to reflect the agent's potential future earnings which are the rewards he was entitled to receive in respect of any benefit that his principal might obtain from his activities. In this type of situation, therefore, the agent should be adequately compensated if he is paid for the value at the date of termination of the business he has built up. However, the position envisaged in sub−paragraph (b) is rather different. If the agency is terminated in circumstances where the agent has not been able to amortize expenses he has incurred on the advice of the principal in setting up the agency, the value attaching to the business may or may not provide sufficient compensation. I see no reason to restrict the meaning of "damage" in those circumstances to loss of goodwill. In my judgment the agent is entitled to recover whatever loss he can show he has suffered which in a case of this kind might consist in whole or in part of the amount of the unamortized expenses.

30. These conclusions rest on the language of the Directive and the Regulations rather than on the practice of courts of other Member States, although to judge from what is said in the Commission's report there is no reason to think that they are inconsistent with the view taken in France, which seems to be the only other country to have adopted the compensation system. They do not necessarily lead to the conclusion that the common law approach to the assessment of damages is to be disregarded altogether, but if one regards the goodwill attaching to a business as a species of property it becomes easier to understand why in the ordinary case questions of mitigation of the kind that would arise if the court were assessing damages for loss of earnings flowing from a breach of contract do not arise and why one is not concerned with what the agent could have done to obtain alternative employment elsewhere.

31. The nature of the entitlement to compensation under Regulation 17(6) was considered in some detail in *King v Tunnock* . The court reached much the same conclusion, holding that a commercial agent is entitled to compensation for the loss of the value of the agency as at the time of termination. Lord Caplan expressed the matter in this way in paragraph 38 of the judgment:

> "Moreover, what is compensated is "the termination of his relations with his principal". The emphasis is not on his future loss but on the impact of the severance of his agency relationship with his principal. An agency generally has commercial value. This is acknowledged by the fact that under Regulation 18(c) the commercial agent may, with the agreement of his principal, assign his agency contract to another."

32. Later, when comparing the entitlement to compensation under paragraph (6) to the entitlement to an indemnity under paragraph (3) he said in paragraph 40 of the judgment:

> ". . . . . compensation is payable upon rupture of the relationship with the principal. At that point of time the value of the lost agency must be ascertained and there is simply no reference to the actual course of events to be expected after the termination. Indemnity hinges upon the principal continuing in business and exploiting the agent's connection. Unless Regulation 17(7) represents a restriction or qualification of 17(6) it is not necessary for the agent to project his actual prospective loss. All he needs to prove is that after termination he had lost the value of an agency asset which, prior to the termination, existed. . . . . If what is lost has little or no value then of course the level of compensation may be fixed at a low level, but that is a different matter."

33. Again, contrasting the terms of paragraph (3) with those of paragraphs (6) and (7), he concluded that it is not a prerequisite to an entitlement to compensation that the principal remain in business. He therefore concluded in paragraph 43 that

> ". . . . . in so far as entitlement to compensation is concerned the Directive is not troubled with what happens after the date of termination. It is the value of the rupture of the agency relationship that is the source and justification of compensation."

34. I would respectfully agree with all those observations.

35. A similar understanding of the effect of the Regulations is reflected in the judgment of Davis J. in *Tigana v Decoro* . One of the issues that arose in that case was whether an agent was entitled to receive compensation under Regulation 17(6) in a case where the agency was expressed to continue for a limited period and expired by effluxion of time. The judge noted that the word "termination" is capable of meaning simply "coming to an end" and that it is used in that sense in regulations 8 (commission on transactions concluded after the agency has terminated) and 20(2) (restraint of trade clauses). He concluded that it was to be given the same meaning in regulation 17(6) so that compensation was payable in such circumstances. One of the reasons he gave for that conclusion in paragraph 77 of the judgment was that

> ". . . . . as the recitals to the Directive show, a principal purpose of the Directive was to afford protection to a commercial agent. Moreover one can discern from the Directive (and Article 17 and Regulation 17 themselves) a desire to prevent a principal from, as it were, unjustly enriching itself by appropriating to itself, without recompense, the goodwill and customer connection to which the efforts of the commercial agent have contributed; and to compensate the agent for the

> loss to him of his agency. There is no identifiable reason for there being an intention that that purpose should not be applicable to agency contracts which expire by effluxion of time: indeed that would seem to involve a major inroad into the protection otherwise designed to be offered."

36. That was endorsed by this court, albeit obiter, in *Light v Ty Europe Ltd* [2003] EWCA Civ 1238, [2003] Eu.L.R. 858 and is entirely consistent with the view that the agent is entitled to receive compensation for the goodwill of the agency which is unaffected by the fact that the relationship between the principal and agent has come to its natural end.

37. In *PJ Pipe v Audco India* , on the other hand, it appears to have been assumed by all concerned that the damage in respect of which an agent is entitled to obtain compensation under regulation 17(6) extends to losses arising from the principal's wrongful repudiation of the agency agreement. In view of the broad wording of the regulation I can understand why that assumption should have been made, but I think there are strong reasons for doubting whether it is correct. One of the main purposes of the Directive was to harmonise the laws among Member States and in the course of doing so to provide additional protection for commercial agents. That suggests that its purpose was to provide a remedy that in some cases would not otherwise be available. It can hardly be supposed, however, that an agent whose contract was wrongfully terminated by his principal would not have had a remedy under the general law of any of the Member States. The very fact that Member States were given the choice of implementing the indemnity or compensation system points to the same conclusion, as do other provisions of Articles 17 and 18. The question is likely to be of importance only insofar as the principles applicable to the assessment of compensation differ significantly from those that apply to the assessment of damages for breach of contract, although for reasons which I will explain in due course, I do not think that they do. However, the question does not arise for decision in this case and it is therefore unnecessary to express a final view on it.

38. With the exception of *Duffen v Frabo* and *PJ Pipe v Audco India* these decisions all point to the same conclusion, namely, that the damage suffered by the agent as a result of the termination of his relations with his principal is normally the loss of the agency business, including whatever goodwill attaches to it. In my judgment that is the correct interpretation of regulation 17(6) and therefore the compensation which the agent is entitled to receive in such cases should reflect the value of the business at the date of the termination. Once that is recognised the task of assessing the amount of compensation in any given case is made easier because the court can concentrate on the facts and matters that have a bearing on the value of the business to the exclusion of those that do not. For example, at one point Mr. Moser sought to argue that compensation could, in an appropriate case, be assessed by reference to the benefit that the principal had obtained from the agent's activities prior to termination or to the value of the agency business at the date of termination, or even both. However, if one is seeking to put a value on the agency business itself, it is difficult to see what relevance can be attached to the benefits obtained by the principal prior to its termination. If the court had power to award the agent whatever amount it

considered to be fair and reasonable in all the circumstances of the case as a form of severance payment, there might be something to be said for taking into account the duration and quality of the agent's performance as well as any enduring benefits to the principal, but in my view that is not what paragraph (6) provides for.

39. In *King v Tunnock* the Court of Session appears to have been attracted by the two years' commission rule adopted by the French courts. Such a rule, even if only adopted as a benchmark or guideline, has the attraction of simplicity and certainty, but in none of the cases to which our attention was drawn has anyone attempted to provide a rational explanation for it and none is offered in the Commission report. I would respectfully agree with the observation made by Davis J. in *Tigana v Decoro* that a broad rule of that kind is inadequate to deal fairly with the range of cases likely to come before the courts, but in my view it is open to the more fundamental objection that it does not involve any reasoned attempt to ascertain the true extent of the agent's loss.

40. Mr. Moser submitted that it is necessary to adopt the two years' commission rule, or something like it, in order to ensure that the agent obtains an effective remedy as required by the decision of the European Court in *Francovich v Italy* [1991] ECR I−5357, but I am unable to accept that submission. Although the preamble to the Directive makes it clear that one of its objects is to enhance the protection given to commercial agents, one can only identify the harm against which it was intended to protect them by examining the language of the Directive itself. In my view Article 17.3 and paragraph 17(6) of the Regulations are reasonably clear in that respect. I accept that the courts must be careful not to impose unrealistic evidential requirements on agents seeking to prove their loss and that in many cases it may be appropriate to adopt a broad approach. However, I can see no basis for construing the Directive or the Regulations in a way that would entitle the court to award an amount of compensation unrelated to the damage which the agent has actually suffered, much less a conventional sum largely unrelated to the particular circumstances of the case. For my own part, therefore, I do not think that the two years' compensation rule can be supported even as a broad guideline.

41. In paragraph 89 of his judgment in *Tigana v Decoro* Davis J. made a valiant attempt to identify the factors which should be taken into account in deciding what compensation, if any, to award. I do not think that it would be helpful to repeat them here, but it is worth noting that they included the period of the agency as provided for in the contract as well as other terms, such as exclusivity, to which it was subject, the actual duration of the relationship, the nature of the market and the client base, the extent to which the principal has continued to enjoy benefits after the termination of the agency as a result of the agent's activities, and the manner of termination. If the court's task were to award a sum which is fair and equitable having regard to all the circumstances of the case, I have little doubt that most or all of these factors would play an important part in any assessment of compensation. However, if, as I think will normally be the case, the court's task is to assess the value of the business to the agent at the date of termination, many of these factors will have little or no part to play and those that do will only be relevant insofar as they shed some light on that question.

42. One factor that was not mentioned by Davis J., but which must be considered in the present case, is the state of the principal's business. In some cases it will be buoyant and in others it will be in decline, but in either case it is likely to affect the value of the agency. It is obvious that the amount that a potential purchaser of an agency would pay to acquire it will depend to a considerable extent on the amount of commission that it can be expected to produce, which in turn will depend in part on the strength of the principal's business. In some cases it may be clear that the business is nearing, or has reached, the point of collapse.

43. This situation arose in *King v Tunnock* where the agency was terminated as a result of the principal's decision to close its bakery business. In the course of analysing the nature of the agent's entitlement to compensation the court drew attention in paragraph 43 of the judgment to the fact that although it is a prerequisite of the entitlement to an indemnity that the principal should continue in business, that is not so in the case of the entitlement to compensation. Lord Caplan said:

> "The vital difference between indemnity provisions and the compensation provisions is that indemnity requires that the principal should continue his business. If the principal does not continue in business after the termination the requirements of Regulation 17(3) cannot be satisfied. In the case of compensation there is no prerequisite to entitlement that the principal continues in business. Thus compensation may arise where, (as in this case), the principal shuts down the relevant part of his business, or say ceases to trade because the company goes into receivership. We can thus conclude that in so far as entitlement to compensation is concerned the Directive is not troubled with what happens after the date of termination. It is the value of the rupture of the agency relationship that is the source and justification of compensation."

44. It is of course true that neither the Directive nor the Regulations make it a precondition to the right of an agent to receive compensation that the principal should continue in business, but I do not think it follows that it is a matter that can be ignored altogether when it comes to assessing compensation. Although I would agree that the value of the rupture of the agency relationship is the source and justification of compensation, in the sense that the damage suffered by the agent is to be assessed by reference to the value of the business of which he is deprived by the termination of the relationship, I do not think that means that the Directive or the Regulations require one to shut one's eyes to what was likely to happen in the future when it comes to assessing compensation.

45. There is no reference in that part of the judgment which deals with the assessment of compensation to the fact that Tunnock had closed its bakery business. The reason for closure is said to have been "a commercial reason", which I presume means that it would not have been profitable to continue it. Having acknowledged that the two years' commission rule is only a benchmark Lord Caplan said in paragraph 51:

> "It makes sense that the earning potential must be a factor in any evaluation of an agency's worth to the agent and this matter is also taken into account under French law. In this case given that the agency generated a certain degree of commission for the agent this particular agency must have been very valuable for an agency of its type. The pursuer had served his customers for many years and that it is likely that the earlier family connection, through his father, cemented his relationship with some customers. Given his age, he could have hoped to continue the agency for a number of years. In these circumstances we consider it likely that the pursuer would have expected and required a relatively high level of compensation to surrender his successful and long−established agency. The compensation would, of course, require to be tied to the commission he was earning. Thus this is a case where we can conclude, even on the limited information that is available that the agent would have expected to receive a capital sum representing at least the total for the last two years of his earnings to be paid before he would voluntarily have given up his agency. We are reassured that under French law compensation of two years commission would be regarded as a standard compensation for loss of an agency, so that it is difficult to believe that in the present case such compensation could be other than reasonable."

46. The explanation for the omission of any reference to the fact that Tunnock had closed its bakery business is to be found in paragraphs 44−48 from which it appears that a passage in a textbook on French commercial law, in which the cessation of business by the principal was said to be of little relevance to the calculation of compensation, together with the knowledge that the compensation system itself was derived from French law led the court to conclude that it should adopt the same approach and ignore altogether the fact that Tunnock had closed its bakery business.

47. At this point I find myself, with all due respect, unable to agree with the court's conclusion. For reasons which I sought to explain earlier, it might be appropriate to disregard a matter of that kind if the court had a broad discretion to award the agent a sum which it considered to be just and equitable in all the circumstances (which may be the way in which the Directive is interpreted in France) but it is difficult to see how it can properly be ignored if one is seeking to compensate him for the loss of the agency business. Moreover, it is not right to assume that subsequent events are relevant only to the common law doctrine of mitigation. The fact is that the perception of the way in which the agency business is likely to develop in the future is bound to affect its value.

48. However, there is at least one type of case in which it is necessary to adopt a purposive approach in order to give effect to the intention of the Directive, namely, where the agency had a limited life and expired by effluxion of time. In that situation it might be said that at the termination of the relationship the agent had nothing he

could sell and that no goodwill attached to the business. However, it is plain, as this court observed in *Light v Ty Europe* , that the Directive is intended to provide a remedy in such cases. In my view the explanation lies in the fact that although the agent had nothing he could sell, he had nonetheless built up a business to which goodwill attached in the ordinary way and which, if the relationship had continued, would have continued to produce profits in the form of commission. When the agency expires the benefit of that goodwill passes to the principal and if he is continuing in business is likely to be of value to him. As I see it, one purpose of the Directive and the Regulations is to enable the agent to obtain the value of the goodwill which he has built up and which would otherwise pass to the principal free of charge.

49. Mr. Moser submitted that the key to solving this problem lay in paragraph (7) of regulation 17 and in particular in the words

> "damage shall be deemed to occur particularly when the termination takes place in . . . . . circumstances which deprive the commercial agent of the commission which *proper performance* of the agency contract would have procured for him . . . . ." (emphasis added).

His argument was that the regulation requires one to assess compensation on the assumption that the contract continued to be performed properly in the way that it had been in the past.

50. I cannot accept this submission. Paragraph (7) is not dealing with the assessment of compensation but with circumstances in which damage is deemed to have occurred so as to give rise to an entitlement to compensation, although no doubt the commission that the agent could have expected to earn in the future will be reflected in the value of the business. Sub−paragraph (a) appears to be concerned with the case in which the principal obtains the benefit of the agent's efforts while depriving him of the opportunity to earn commission to which he was morally, if not legally, entitled. I think the reference to "proper performance" is simply intended to draw a distinction between what has taken place and what the agent was reasonably entitled to expect. It clearly contemplates circumstances in which the principal continues in business and obtains the benefit of the agent's efforts for himself without paying commission. In my view it has no bearing on the present problem.

51. Mr. Segal submitted that some guidance on the assessment of compensation could be obtained from paragraph (4) of regulation 17 which limits the amount of the indemnity to a maximum of one year's commission. His argument was that if one of the purposes of the Directive was to promote a degree of harmonisation between the laws applicable in different Member States, the Council cannot have intended the amount payable by way of compensation to differ widely from that payable by way of an indemnity.

52. I do not find that argument persuasive. It is apparent from the Commission's report that the Directive represented a compromise between different Member States in which different systems of protection were already in place. It is clear from the language of the Directive itself that the indemnity system and the compensation system operate in different ways and may give rise to different results. The degree of harmonisation which the Council sought to introduce was therefore limited to ensuring that one or other system applied throughout the Community. I can see no reason for thinking that the scope of the provisions relating to compensation was intended to be limited by reference to those relating to indemnity.

53. In the present case it was agreed before the judge that the damage in respect of which Mr. Lonsdale was entitled to receive compensation was the loss of the goodwill attaching to his agency. The judge accepted that and referred to the decisions in *King v Tunnock* and *Tigana v Decoro* as supporting that conclusion. He found that Mr. Lonsdale was a respectably competent, though not outstanding, agent. In paragraph 18 of his judgment he said:

> "If it is kept in mind that the damage for which the agent is to be compensated consists in the loss of the value or goodwill he can be said to have possessed in the agency, then it can be seen that valuation ought to be reasonably straightforward. Small businesses of all kinds are daily being bought and sold and a major element in the composition of their price will be a valuation of goodwill."

54. It will be apparent from what I have said earlier in this judgment that in my view the judge was right to approach the matter in this way.

55. The judge then noted that neither side had put before him any evidence of how commercial goodwill is conventionally valued or any evidence of its value in this particular case. He therefore proceeded to make an assessment by reference to such material as was before him which included evidence of the amount provided by the defendant of the amount of commission that Mr. Lonsdale had earned in each of the six calendar years immediately preceding the termination of the agency in June 2003. It showed that his gross commission had fallen from £18,416 in 1998 to £10,825 in 2002. Howard & Hallam had announced in January 2003 that its business would close at the end of June. The defendant's records show that Mr. Lonsdale's commission for 2003 was £7,139. Mr. Lonsdale's own records for the financial years ending 5th April 2000 to 5th April 2003 indicate that his commission declined over that period from £12,410 to £9,230 and that for the six months to October 2003 it fell to £4,177. The agent who had taken over Mr. Lonsdale's area following the sale by Howard & Hallam of its business gave evidence that there had been a significant reduction in sales.

56. In the light of the evidence before him the judge concluded that at the time the agency was terminated Howard & Hallam's business had been in serious decline. He pointed out that the agency was producing a modest and falling income in a steadily deteriorating environment and doubted whether anyone in those circumstances would

have been willing to pay as much as two years' gross commission based on historical figures in order to acquire it. There was no evidence that anyone would have paid anything to buy it or that Mr. Lonsdale could realistically have expected to be able to sell it. In the end he assessed compensation at £5,000.

57. Mr. Moser challenged the judge's decision both on the grounds that he had failed to apply the two years' commission guideline and on the grounds that he had failed to give sufficient weight to the duration of the agency (in this case 13œ years) or the fact that Mr. Lonsdale had performed satisfactorily. However, for the reasons I have already given, I do not think that either of those criticisms is well founded. I am unable to accept that there is or should be any guideline of the kind suggested by Mr. Moser; nor do I think that the duration of the agency or the quality of the agent's performance are necessarily important factors. Whatever the period of the agency in this case, and however well Mr. Lonsdale had performed, nothing could alter the fact that Howard & Hallam's business was in decline and with it the prospects for the agency. The judge was placed in a difficult position in this case because he was provided with very little material on which to base his decision and the valuation of commercial goodwill is not a matter with which he could be expected to be familiar. In most cases the court is likely to benefit from having the assistance of an expert witness (ideally a single joint expert) who can give evidence about the appropriate way of valuing a business of this kind, but I should not wish to encourage the view that that will always be necessary since in some cases the amount in issue will be too small to make that a sensible or proportionate course. If the parties cannot reach agreement it may be sufficient to place all the material before the court and invite the judge to make whatever he considers to be the appropriate order, as the parties did in this case. In such a case the judge is entitled to apply his common sense and adopt a broad brush approach.

58. In my view the judge's decision in this case cannot be faulted. He directed himself correctly on the principles to be applied. He was right to take into account the fact that the business of Howard & Hallam was in serious decline at the time of the termination of the agency since that inevitably affected the value of the goodwill attaching to it. Although his award of compensation reflected a very broad brush approach, I do not think that it can be said to be clearly too low in the light of the evidence before him. I would therefore dismiss this appeal.

Lady Justice Hallett:

59. I agree.

Lord Justice Jacob:

60. I also agree.