

# Minimizing The Risks Of Termination: Doing It Right

Roberta F. Howell



In the [first](#) [1] and [second](#) [2] columns of this series, we discussed how to minimize the risks inherent in terminating a distribution relationship by maximizing the possibility that termination could be avoided altogether. No matter how carefully the relationship is created, structured or nurtured, however, termination is sometimes necessary. Thus, this last column in the series discusses how termination can be implemented to minimize the risks of litigation and enhance the likelihood of a smooth transition.

Making sure that the termination is done properly is, at bottom, answering some of the same questions that any good journalist would ask: when, why, who and how? When can you terminate, why are you doing so, who must you tell, and how should you tell them?

The first place to look to begin answering these questions is the distribution contract. Most written contracts contain language indicating how long a contract is intended to last, when it may or must be renewed, what kind of notice must be provided in advance of termination, whether that notice is different in different circumstances, to whom and how it must be delivered, etc. The easiest way for a distributor who wants to challenge termination to resist is if the termination violates an express contractual provision. So make sure to comply with any such requirements.

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Do not stop there, however. As explained in the last column, many states have statutes that govern the termination of distribution relationships generally, in particular industries, or both. In most cases, that language trumps the contract and is mandatory even if the contract would allow for immediate termination. If it is possible to comply with both the contract and statute, by all means do so. If they conflict, the statute will govern.

Even in the absence of express contractual or statutory requirements, termination is likely not unrestricted. The UCC requires reasonable notice be given and the implied duty of good faith and fair dealing, inherent in every contract, must also be taken into account. Indeed, it is in precisely those situations where there is no governing statutory or contractual provision that the implied duty is strongest. Unfortunately, the requirements of the implied duty may not be entirely clear. Industry practice, prior course of dealings and garden-variety reasonableness are all relevant.

### ***When?***

When termination can be accomplished is often the easiest question to answer. Many contracts have a specified duration. Another common provision is a so-called “evergreen” clause, which provides, for example, that the contract is for a term of one year, but will automatically renew for successive one year terms unless one or both of the parties takes a specified action, usually in the form of some kind of advance notice of an intention not to renew. Similarly, most state statutes governing distribution relationships also expressly delineate the amount of notice that must be provided before termination is allowed. Unfortunately, the amount of notice required often varies, depending on the reasons or circumstances of termination, and is it not uncommon that more than one may apply in a particular situation. Usually, the best practice is to simply give the longest notice arguably required by the contract or statute. No matter how loudly the field sales staff protest, there is usually no harm in waiting a couple of extra weeks for the termination to take effect, particularly if it avoids a basis for long, protracted and expensive litigation. There are, of course, exceptions to that rule, but most often patience truly is a virtue.

### ***Why?***

The notice of termination should explain the reasons for the termination. Even where the contract clearly allows for termination without cause, it is still usually a good idea to explain, particularly if there is a possibility of litigation. Further, many statutes require good cause for termination and mandate that the notice identify the grounds. Regardless, if a judge or jury understands that the termination was done for a good reason, it is not going to look for reasons to give to the terminated dealer a large damage award. There is a fine line, however, between explaining and being defensive. The reasons given should be accurate, documented and significant. Be complete, but don't go overboard. Nit picking is often worse than no explanation at all, but reasons that are not given in a notice of termination will generally not be considered later on as a justification for termination. If significant additional information comes to light after the notice is sent, however, the notice

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may, and usually should, be amended to address those additional grounds.

It is also important to determine whether (a) the contract or applicable statute require that the dealer be given an opportunity to cure before termination, and (b) if so, that the timing and substance of any cure requirement be reasonable and clearly delineated.

### ***Who and How?***

As simple as it may seem, one requirement that often jeopardizes an otherwise proper termination is the manner in which the notice is delivered and the person to whom it is addressed. Again, the contract is the first place to look because, particularly in older contracts, that is where the requirement of registered or certified mail, for example, is likely to be found. Most statutes simply require that the notice be in writing and do not otherwise specify the means for delivery, but that is not always true, so the statute should always be checked as well. The requirements of the contract or statute will likely not be onerous, but they may be mandatory. Failure to ensure compliance is a completely avoidable risk.

### ***Miscellaneous***

In many contracts and, particularly, in dealership statutes for industries where the dealer is likely to have a significant investment in inventory (e.g. construction and farm equipment dealerships), there may be a requirement that the manufacturer repurchase goods remaining in the dealer's inventory at termination. Many statutes also mandate the amount of credit that the dealer must be provided, and may provide that repurchase is at the dealer's option. Even where not required by contract or statute, however, many manufacturers choose to repurchase inventory (at least new and relatively current models) to avoid, e.g., the problems that might result if the dealer simply dumps the inventory post-termination at below cost. In any event, it can sometimes significantly reduce the amount of exposure for a wrongful termination claim and generate a positive reaction by a jury or judge if the manufacturer offers to repurchase the terminated dealer's inventory

Make sure that any post-termination obligations are addressed. That may include the return of signage or specialized tools or marketing materials, price lists, etc. It may also include post-termination non-competes, control of phone book listings or numbers, operating manuals, and the like. Accounts receivable and payable will also have to be reconciled and if not carefully considered in the period leading up to termination may provide powerful leverage to one or the other of the parties in negotiating the transition.

Don't discuss the pending termination with customers, other dealers, etc. Until the termination is effective, transitional issues must be carefully handled to avoid claims by the terminated dealer of interference with its contractual relationships, conspiracy and the like. Those within the company who deal with the dealer, however, need to be aware of what is happening to ensure a consistent message to the outgoing dealer and the marketplace.

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Last, but not least, stop selling to the dealer when the termination is to become effective. While seemingly obvious, it is shocking how often that does not happen, creating wholly unnecessary confusion and opening the door to potential claims that would never have existed otherwise.

Breaking up *is* hard to do. It can, and sometimes must, be done, however. If that reality is recognized, and the process approached with deliberation, caution and a cool head, the result will be far less painful for all of the parties involved.

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