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Overcoming Adverse Contractual Terms:

Does Action Speak Louder Than Words?

When faced with an adverse decision or action by a supplier the first inclination of most distributors (and most attorneys for distributors) is to review their written agreement. This is certainly an appropriate and expected reaction. The question, however, is what should you do if the written agreement appears to support the action contemplated by the supplier?

Suppose, for example, that you get a letter from a supplier that says it intends to appoint another distributor in your territory. You dig out your written agreement and to your dismay there, in black and white, the agreement states that the supplier may appoint other distributors in the territory. You quickly call your lawyer who confirms your reading of the particular clause. Your heart sinks and your stomach churns as you begin to calculate the effects of the inevitable lost revenue that you are facing. Angrily, you mutter under your breath that for 25 years you've built the goodwill of the brand as the only distributor in the territory and that you are not going to take this sitting down. But, you say to yourself, your contract says that the supplier can appoint another distributor in your territory. What can you possibly do?

The answer is simple; look beyond your contract. While the written agreement between parties is certainly the most logical starting point in any analysis of the rights

and obligations of these parties, it is just that - a starting point. In fact there are many factors which affect the ultimate legal relationship of the parties. We refer to these other factors as a distributors "bundle of rights". Included in this bundle of rights, are rights which arise by reason of statutory law, case law, oral agreements between the parties and the parties conduct. This article will focus on the last of these issues - the parties conduct. The parties conduct is frequently overlooked when analyzing the parties' respective rights and, as we shall see, the parties' actual conduct as opposed to the written agreement between the parties, may ultimately rule the day.

What Is Your Agreement?

While there are many beer franchise statutes that apply to the relationship between supplier and distributor, these statutes are, for the most part, relatively limited in scope. That does not mean, however, that if your state's beer franchise statute is silent on a particular issue (such as the right to dual distributors in our example) that there is no statutory law which may be invoked to assist the wholesaler. To the contrary, there are many other statutes which may apply. The most important of these statutes is the Uniform Commercial Code ("UCC").

The UCC, although subject to variation from state to state is, as the name suggests, a fairly uniform system of laws throughout the country (excluding Louisiana) which, among other things, governs the relationship between all suppliers and distributors of goods. Under

the UCC, an "agreement" is defined as "the bargain of the parties in fact as found in their language or by implication from other circumstances, including, course of dealing or usage of trade or course of performance." What this means is that the written agreement (the language of the parties) is only a part of the picture when it comes to determining what the parties' agreement is. According to the UCC, in order to determine what the parties' actual agreement is you have to look beyond the written (or spoken) words, to the parties' actual conduct.

Turning back to our example, when the distributor which for 25 years had been the exclusive distributor in its territory, received notice of the supplier's decision to appoint another distributor, the appropriate inquiry was not "What does your contract say?" but, rather "What is your agreement?" Now you know that to answer the question may not be identical. In order to determine what the parties' agreement is you may have to go beyond the written contract and include the parties' actual performance.

Course of Performance and Course of Dealing.

During the course of any long-term sales relationship parties tend to develop particular ways of doing business. Over time relationships change and so do business operations. Written agreements which may have been signed in contemplation of one particular set of circumstances may over time bear little relevance to present realities. Other times, written agreements may be drafted after the parties' relationship and their methods of operations have matured which may not appropriately reflect the parties' agreement relating to particular issues as evidenced by their actual performance.

In order to avoid the elevation of form over substance or, more specifically, in an attempt to recognize what the parties' actual agreement is, two key concepts have developed under the UCC; course of performance and course of dealing. In essence, course of dealing relates to conduct between the parties prior to entering into an agreement while course of performance focuses on the conduct of parties after a contract has been entered into. Both course of dealing and course of performance may be used as evidence to explain, supplement or qualify the terms of a written agreement, while course of performance may be used to demonstrate a waiver or modification of a written agreement. The cornerstone of both of these prin-

ciples is that the parties' conduct is often the best expression of what their agreement actually is.

Conflicts between Conduct and Contract

So, now you know that your agreement is not necessarily limited to the four corners of your written distribution agreement. But, to go back to our example, you are still holding your agreement in your hand and reading the language that says the supplier can appoint other distributors in your territory. "It's clear as day", your attorney says, "a six year old can understand the language". Are you cooked? Well certainly your supplier will make that argument. The fact is, however, that the agreement is certainly strong evidence, but it is not dispositive. That is because a course of performance - conduct after the agreement has been signed, may still be used to show a waiver or modification of the agreement.

In other words, sticking with our example, since the distributor had in fact been exclusive in the territory for 25 years - despite the presence of the clause permitting the supplier to dual him - a strong argument exists that the parties by their performance have created an exclusive distributorship.

The ultimate determination on any such issue will be highly fact sensitive and will involve various other legal arguments as well, on both sides of the table. The important point to keep in mind is this: just because your written contract says something does not necessarily mean that it is enforceable. The review of your contract is a starting point, not the end of your inquiry.

Practical Applications of the Course of Performance Doctrine

As already demonstrated, one practical application of the course of performance doctrine relates to exclusivity. Many distributors who have enjoyed exclusive distribution rights may be at risk of having those rights diluted because of contractual language with either expressly permits a supplier to appoint other distributors to sell directly in a territory or because the granting language is either less than specific or conveys something less than exclusive rights.

Clearly, there is a legal distinction between being appointed as an "exclusive distributor" and being appointed merely as "a distributor" in a given territory. Perhaps it is not as apparent, but there is also a legal distinction with being appointed as an "exclusive

distributor" and with being granted the "exclusive distribution rights" to a particular product. For purposes of this article, suffice it to say that in any scenario other than where the distributor is granted exclusive distribution rights, a supplier may argue that it has the right to either sell directly or appoint other distributors. While this certainly highlights the need to pay close attention to such language when asked to sign a distribution agreement, regardless of the language of the contract a distributor may buttress its claim of exclusivity with evidence demonstrating actual exclusivity over a period of time.

Another significant area for application of this concept is with respect to "add-on" brands. Many distribution agreements are limited to a finite group of products as specified on a schedule to the agreement. Other agreements specifically disclaim the right of the distributor to new products released by the supplier or to line extensions. In those situations where a supplier for one reason or another does not want to give a new product or line-extension to its existing distributor in a given territory, the supplier will inevitably point to such language in their agreements to support their decision to give the product to one of your competitors. While such conduct raises numerous issues which are beyond the scope of the present article, a prior course of performance pursuant to which the supplier did consistently provide a distributor with new products and line extensions will certainly support an argument that the contract has been modified or the applicable provisions waived.

Conclusion

At the risk of being redundant, we can not overemphasize the need to be vigilant with respect to your legal affairs. Pay attention to your distribution agreements when they are presented for signature. Don't just play the sign and return game. Your agreements are an important and primary source of your rights and obligations. As such, as issues arise, they are the first reference source to determine your rights. However, if you remember even one thing from this article, let it be that your written agreements are only a part of your bundle of rights as distributors. As such, the final word on any particular issue may not be contained within your agreement and may even be contrary to the written word. Always look beyond your agreements, and always consider what your actual conduct has been with respect to any particular issue. After all, what is more indicative of the parties' intent than their conduct? ■