CLIFFORD CHANCE

Newsletter no. 1 –Commercial Contracts

February 2014

Distribution: two important judgments on the concept of significant imbalance

In two recent judgments the Paris Appeal Court has outlined the concept of significant imbalance in relations between suppliers and distributors, with the latter being dispensed from sanctions if they can prove that they effectively negotiated the clause at issue. ***To find out more…***

The sudden breaking-off of established commercial relations recognized as a public order act

In a judgment by the Versailles Appeal Court dated 29 October 2013, the judges expressly acknowledged the public order act nature of Article L. 442-6, I, 5° of the Commercial Code and confirmed the tortious nature of liability incurred pursuant to the same Article. ***To find out more…***

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Distribution: two important judgments on the concept of significant imbalance

Article L.442-6, paragraph 1, indent 2 of the Commercial Code prohibits subjecting or attempting to subject a commercial partner to commercial practices entailing significant imbalance in rights and duties between the parties. The General Directorate for Competition, Consumer Affairs and Elimination of Fraud ("**DGCCRF**") representing the Minister with responsibility for the Economy has the power to ask the courts to put an end to such practices, to set aside illicit clauses, to order restitution of monies paid without due cause, to inflict a civil fine of up to two million Euros, an amount that may potentially be increased to three times the amount paid over without good cause and, additionally, to order remedy for losses suffered by suppliers. The lack of any legal definition of "significant imbalance" makes it of prime importance to analyse the judgments handed down by the Paris Appeal Court, the only higher court enjoying jurisdiction for this type of dispute. The two judgments firstly restated the decision of the Constitutional Council regarding the preliminary question of constitutionality of 13 January 2011 stating that *"the legislator made reference to the legal concept of significant imbalance in the rights and duties between the parties that is to be found in Article L. 132-1 of the Code of Consumer Law restating the terms of Article 3 of Directive 93/13/EEC of the Council dated 5 April 1993"* and that it is for the court to give judgment in the light of the existing consumer law case law. It is also established by the judgments commented upon that this is undertaken in two stages in which either party successively inherits the onus of proof:

1. it is firstly demonstrated that the agreement at issue is significantly out of balance, i.e., pursuant to the judgments commented upon, that it contains one of more obligations that are "*unjustifiably borne by the supplier and prejudicial to the Economy (and to consumers)*“. In the case in point, disproportion was noted between the obligations placed on the parties, a practice similar to one of those strictly prohibited by the Code of Consumer Law, or, in other words, a clause so drafted as to allow one of the parties to arbitrarily penalize the other.
2. the party presumed to be at fault can then disclaim liability by providing proof of the effectively negotiated nature of the provision at issue, in particular by justifying another clause that would result in restoring balance to the relationship.

It was in this way that the Paris Appeal Court, in a judgment dated 18 September 2013, fined the GALEC co-operative two million Euros for having attempted to get its suppliers to waive their right to remedy resulting from a previous judgment against the distributor. The Court reminded the parties that clauses requiring consumers to reduce their rights to remedy or to refer a matter to the courts represent unfair clauses under consumer law , that "*these* [consumer law] *rules may found application of Article L 442-6, I, 2 of the Commercial Code"* and that GALEC did not demonstrate that such imbalance had been compensated by consideration or that it had formed part "*of the economics of its relations with its suppliers*".

Eurauchan, for its part, saw in a judgment dated 11 September 2013, the upholding of its sentence to a civil fine of one million Euros for having added to its annual distribution agreement the following:

- a price-review clause providing that the price was to be automatically renegotiated in the event of a technical lowering of the supplier's prices or raw-material prices but required the supplier, prior to seeking a price rise, to provide evidence of the objective factors on the basis of which he intended to proceed to increase prices but in the absence of any definition of the said objective factors. The distributor was thus able to freeze prices for a considerable lapse of time or, again, negotiate new terms and conditions of sale that could then wipe out the price increase ;
- a clause providing for a system of penalties in the event of suppliers' failure to meet a minimum 98.5% service rate to penalize deliveries that did not comply with the term and conditions set out in the order. This service rate was criticized for not taking into account the suppliers' specific activities and because, as the criterion triggering the said right was not defined, the possibility of seeing this right actuated could represent a threat when the following single agreement was negotiated.

These two decisions underline the fact that prohibition of significant imbalance in relations between supplier and distributor is aimed at enabling suppliers to negotiate on a clause-by-clause basis the agreements binding them to distributors.

The case law is becoming clearer and clearer in outline. Consequently, commercial negotiations should be guided by a quest for overall balance between the rights and duties of parties so that evidence of genuine negotiation can be established.

CA Paris 11 September 2013 no. 11/17941, Minister for the Economy versus Eurauchan ch. 5-4

The sudden breaking-off of established commercial relations recognized as a public order act

In the case in point, a German company informed its French distributor of its intention to break off commercial relations which had lasted 25 years. The letter so intimating gave 11 months' notice. Challenging the notice period, the distributor summoned the German company to appear before the French courts pursuant to Article L. 442-6, I, 5, of the Commercial Code relating to wrongful breaking-off of established commercial relations. The claim was granted at first instance and the judge set a notice period of two years and granted the distributor 2, 900,000 Euros in damages (Pontoise Comm. Co., 2 February 2012).

At appeal, the German court requested the court to decline jurisdiction in favour of the German courts pursuant to a jurisdiction clause appearing on its invoices. However, as the French distributor noted, the jurisdiction clause was not properly brought to the latter's attention as it appeared at the bottom of invoices in small print, in German and amidst the supplier's details. This argument was approved by Versailles Appeal Court, which invalidated the clause.

The jurisdiction clause having been invalidated, the court had to find which courts had jurisdiction. In order to be able to accept jurisdiction and deprive the German courts thereof, the Versailles Appeal Court recognized the sudden breaking-off of established commercial relations within the meaning of Article L. 442-6, I, 5, of the Commercial Court as a public order act. This was because it held that "*Article L. 442-6, I,5, of the Commercial Code is recognized as a public order act within the meaning of Article 3 of the Civil Code and is a rule that obligatorily binds the French courts.*"

Furthermore, the question was put whether the applicable law was determined from the nature of the action undertaken pursuant to Article L. 442-6, I, 5, of the Commercial Code. According to the German company, the action was contractual in nature. Given this, the law applicable to the dispute was German law. The Versailles Appeal Court rejected this argument and confirmed that liability incurred pursuant Article L. 442-6, I, 5, of the Commercial Code was tortious in nature.

Consequently, in the absence of any applicable-law clause and given the action for tortious liability brought against the tortfeasor, the law to be applied was that of the place where the prejudice occurred which, in the case in point, was France, with the result that French law should apply and, in particular "*Article L.442-6 I, 5, of the Commercial Code which is a rule defending economic public order, recognized as a public order act within the meaning of private international law*".

Vigilance is essential within the framework of international relations when drafting jurisdiction clauses and applicable law clauses.

Versailles Appeal Court, 12th Div., 12/01461, 29 October 2013, Lauterback versus SA Logic Instrument

In brief…

Judicial summary of practices examined by the DGCCRF.

The General Directorate for Competition, Consumer Affairs and the Elimination of Fraud ("**DGCCRF**") has recently published its civil and criminal judicial summary for 2012.

In it are summarized a large number of judgments mostly handed down by the civil and criminal courts at first instance. It also gives details of the amounts of fines levied.

The following decisions in particular are contained in it, setting out:

- that three months' notice given by a company to its supplier was sufficient given the derisory nature of the shared turnover achieved, which was of the order of 1% (**Paris Commercial Court, 13 February 2012**);
- that a company which had recourse to bartering with other resellers in order to have in stock the full range of telephone cards should be sanctioned. Even if the exchanges involved no monetary transaction, the Court held that such practices constituted selling and that, this being so, the lack of billing was in breach of the provisions of Article L. 441-3 of the Commercial Code. (**Paris Appeal Court, 22 October 2012**);
- that selling at a loss was prohibited in the case of a company that argued the existence of credit notes previously issued by the supplier as the said notes could not be included in the sales invoice insofar as this option is offered by the Commercial Code "*only in the event of restocking with products with the very same characteristics*" (**Strasbourg Civil Court, 3April 2012**).

The DGCCRF has also specified that most of the offences recorded related to breaches involving rules (failure to precisely identify the product sold, off-bill rebates and malpractices involving self-billing procedures and post-dating invoices) and payment dates, the subject of criminal-law sanctions (transport services and for sales of meat, perishables and alcoholic drinks).

Civil and Criminal Judicial Summary 2012

The fine line between the illicit lending of employees and a commercial contract.

Article L. 8241-1 of the Code of Employment Law states that, except where legal, any profit-making transaction the sole aim of which is to lend one's workforce is prohibited. In a judgment dated 10 September 2013, the Commercial Division of the Supreme Court gave an illustration of the distinction between the prohibited practice of workforce lending and commercial agreements giving rise in actuality to the provision of staff, which are authorised. In the case in point, technical skills were imparted and the staff provided remained under the orders and control of their employer, a fact which enabled the transaction performed between the parties to be described as a sub-contracting agreement and not as the illicit lending of employees.

Cass. com., 12-18050, 10/09/2013, APV versus Société CCA Secours

Can an Internet site be regarded as a new point of sale?

In 2006, two companies concluded a franchising agreement for the running of a motorbike accessories shop. The franchising agreement contained a sales territory exclusivity clause under which the franchisor had undertaken not to set up another franchised point of sale within the sales territory granted to the franchisee.

The franchisor subsequently opened a website to sell his products and distribute catalogues mentioning his internet details with lower prices and product delivery at the franchisee, who was not remunerated.

The franchisor was sued with a view to termination of the franchising agreement and for the payment of damages.

The question posed was then whether the franchisor, who had granted sales territory exclusivity to a franchisee breached such exclusivity by opening an internet site and whether the latter was or was not a point of sale.

In a judgment dated 5 October 2011, the Aix-en-Provence Appeal Court answered this question positively. The Court terminated the franchising agreement, finding against the franchisor and ordering him to pay damages to his franchisee.

Conversely, in a judgment dated 10 September 2013, the Supreme Court set aside the judgment in appeal pursuant to Article 1134 of the Civil Code. The Court found that "*the agreement limited itself to guaranteeing the franchisee, […], sales territory exclusivity in a determined sector and that the setting up of a website could not be assimilated to setting up a point of sale within the protected sector".*

In other words, the Supreme Court held that the setting up of a website by the franchisor could not be regarded as a new point of sale within the protected sector.

It should not be forgotten that this view results from an unbroken line of precedents since as early as 2006 three judgments confirmed that the setting up of a website could not be assimilated to setting up a point of sale in a protected sector.

Cass. com., 12-11701, 10/09/2013, Mad Bike versus GSR

The Consumers Bill or Hamon Bill.

We devoted an article to the consumer affairs bill ("**Hamon Bill**") in our last publication. Since then, the ***text*** was adopted BY The National Assembly on 16 December 2013 and forwarded to the Senate.

The Senate's Commission for Economic Affairs examined the text at its second reading and adopted the report of Mr Martial Bourquin and Mr Alain Fauconnier.

The main amendments made to the text by the Commission for Economic Affairs were the following:

- restore Article 1 relating to the arrangements for simplified class action as adopted by the Senate at the first reading, which were more precise and legally safer;

- opt for simplified class action only when the identity and number of affected consumers are known and have suffered losses of the same amount (***Amendment COM-76***);

- instigate class action to obtain remedy for losses suffered by consumers through the failure of a single professional to fulfill his obligations (***Amendment COM-75***);

- remove the new promotional instruments (NIP) from the scope of the single agreement (***Amendment COM-98***);

- keep the possibility for an overall reduction relating to the "other obligations" placed upon the distributor with regard to his supplier (***Amendment COM-94***) ;

- bring in the notion of wrongful practice in the provision forbidding the practice of "margin guarantees" (***Amendment COM-96***) ;

- strike out from Article L. 441-7 of the Commercial Code the information that the supplier's price list included in his general terms and conditions of sale (CGV), and communicated prior thereto, would be mentioned in the single agreement "*for information purposes"* (***Amendment COM-97***).

Since then, the text has been discussed at its second and final reading in the Senate on 27, 28 and 29 January 2014. It was adopted with amendments on the basis on the report by Martial Bourquin and Alain Fauconnier, by 189 votes to 137.

It is envisaged that the Prime Minister will call a joint bilateral commission composed of seven members of parliament and seven senators. This commission will be given the task of finding compromise wordings for all the articles which remain at the discussion stage. The law could be promulgated in March.

We will of course keep you informed of future progress.

Minor Law (29 January 2014)

Comprehensive Report of Proceedings at the public session (27 January 2014) ; analytical report on ***28*** and ***29*** January 2014 – public ***ballots***

Report no. 282 (2013-2014) of Mssrs. Martial BOURQUIN and Alain FAUCONNIER, drafted for and on behalf of the Commission for Economic Affairs, lodged on 15 January 2014 (put on line on 20 January 2014)

Text of the Commission no. 283 (2013-2014) lodged on 15 January 2014 (put on line on 20 January 2014)

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