



French Distribution Law Update

# FRENCH DISTRIBUTION LAW

## NOVEMBER 2018 UPDATE





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# CHAPTER 1

## INTRODUCTION

### Section 2 Vertical restraints put to the test of economic analysis

#### II. Economic theory and competition law

##### 1.09. New generation block exemption regulations.

Over the last ten or so years, influenced by the economic analysis of vertical restraints, the Commission has clearly affirmed its desire to adopt an economic and less formalistic approach when implementing its block exemption regulations<sup>1</sup>. This effects-based approach, announced in the Green Paper on competition policy and vertical restraints of 22 January 2007, was the inspiration for block exemption regulations No 2790/1999 and 330/2010 and also the motor vehicle BER No 1400/2002, and their guidelines<sup>2</sup>.

The effects-based approach consists in particular of the acknowledgment of the particularism of vertical relations, the determining of whether the exemption applies according to the market power of operators - measured in terms of market share, and the importance accorded to operators' economic freedom as well as their self-regulation.

The guidelines on vertical restraints<sup>3</sup> published by the Commission codify much of the economic analysis of vertical relationships and the principal axioms of economic theory are clearly enunciated in them - "For most vertical restraints, competition concerns can only arise if there is insufficient competition at one or more levels of trade, that is, if there is some degree of market power at the level of the supplier or the buyer or at both levels. Vertical restraints are generally less harmful than horizontal restraints and may provide substantial scope for efficiencies"<sup>4</sup>. The criteria for legal assessment also

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<sup>1</sup> See Guidelines on Vertical Restraints No 2000/C 291/01, par. 102: "In the assessment of individual cases, the Commission will adopt an economic approach in the application of Article [101 TFEU] to vertical restraints. This will limit the scope of application of Article [101 TFEU] to undertakings holding a certain degree of market power where inter-brand competition may be insufficient".

<sup>2</sup> Guidelines on Vertical Restraints No 2010/C 130/01, par. 97: "In the assessment of individual cases, the Commission will take, as appropriate, both actual and likely effects into account. For vertical agreements to be restrictive of competition by effect they must affect actual or potential competition to such an extent that on the relevant market negative effects on prices, output, innovation, or the variety or quality of goods and services can be expected with a reasonable degree of probability".

<sup>3</sup> OJEU 2010/C 130/01 of 19 May 2010.

<sup>4</sup> Guidelines on Vertical Restraints, par. 6.



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closely follow the economic theory of vertical restraints - "The assessment of whether a vertical agreement has the effect of restricting competition will be made by comparing the actual or likely future situation on the relevant market with the vertical restraints in place with the situation that would prevail in the absence of the vertical restraints in the agreement. In the assessment of individual cases, the Commission will take, as appropriate, both actual and likely effects into account"<sup>5</sup>.

When the first vertical restraints regulation was adopted, the Commission set the maximum market share threshold at 30% for suppliers to be eligible for the block exemption (except in the highly theoretical case of exclusive supply contracts where the buyer's market share would be used). Under the new vertical restraints regulation (No 330/2010), the exemption is subject to a double market share threshold of 30% - assessed respectively for the supplier on the downstream distribution market and the distributor on the upstream purchase market. The market share threshold is therefore used to assess both the supplier's market power and the distributor's buyer power.

The consequence of the move from a legalistic, prescriptive and standardized block exemption system - providing in detail those contract terms that are prohibited, those that may prove difficult and authorized terms - to a system of moderately supervised freedom based on an economic approach means that operators are responsible for self-assessing their agreements. They must evaluate their market share and determine whether or not it exceeds the dual 30% threshold, and ensure that their agreement or the market situation are not such as to expose them to a withdrawal of the exemption, and if over the "safe harbor" threshold, they must carry out their own assessment of the vertical agreements in light of the EU competition rules. The guidelines are to provide assistance for operators in respect of this self-assessment<sup>6</sup>.

The effects-based approach adopted in the vertical restraints regulations were the inspiration for all the second generation BERs, particularly the Motor Vehicle BER No 1400/2002 and Regulation No 772/2004 on technology transfer agreements.

For matters relating to motor vehicles, the Commission has clearly demonstrated its wish to have a more flexible set of rules than those set out in the previous regulation, No 1475/95. Regulation No 1400/2002 was, "less prescriptive than Regulation No 1475/95, with a view to avoiding the "straitjacket" effect [...] and to allow the development of innovative distribution formats"<sup>7</sup>. According to the Commission, it was

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<sup>5</sup> Guidelines on Vertical Restraints, par. 97.

<sup>6</sup> Guidelines on Vertical Restraints, par. 3.

<sup>7</sup> Explanatory Brochure, 10, par. 3, LawLex2008000066JBA.



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based "on a more economic approach and on the principle that it is for the economic operators (manufacturers, dealers) to organise distribution according to their own needs". Various characteristics can illustrate how the Motor Vehicle Regulation has taken on board the economic approach:

- determination of the exemption according to market share threshold (30% in general and 40% for quantitative selective distribution of new vehicles);
- adoption of the general structure of the vertical restraints regulation, avoiding as far as possible the listing of mandatory provisions: only hardcore restrictions leading to the withdrawal of the exemption for the whole of the agreement and "red clauses" opposing the exemption of the obligation in question are still present; white and gray clauses have disappeared altogether;
- the choice offered between different types of distribution - qualitative, quantitative and quantitative, or exclusive - for new vehicles;
- the variety of possible contract models for the organization of sales and after-sales, subject to compliance with the provisions of the regulation.

However, unlike the vertical restraints regulation which adopted a purely economic approach, the motor vehicle regulation combined that approach with the establishing of a veritable status for distributors. Exemption thus depended on standards which had no direct link with competition and are in fact concerned with the protection of competitors. In addition, there were many more conditions of applicability of the exemption than in the vertical restraints regulation, as well as more "black" and "red" clauses. Operators' freedom of choice was often illusory. For the distribution of new vehicles, the choice of the qualitative and quantitative selective distribution model was virtually obligatory.

During the evaluation of Regulation No 1400/2002, the Commission found there were perverse effects for many of the rules specific to the automobile sector that were absent from general regulation. It argued in favor of a return of the industry to the general vertical restraints regime. However, due to the considerable resistance of automobile distributors and repairers, it was forced to defer application of the vertical restraints regulation to motor vehicles by three years and adopt a hybrid regime: after-sales came under Vertical Restraints Regulation No 330/2010 from 1 June 2010 but Regulation No 1400/2002 continued to apply to new vehicle sales until 1 June 2013.

Due to the expiry of the Vertical Restraints Regulation in 2022, the Commission has initiated an evaluation procedure (Evaluation Roadmap of 8 November 2018) in order to determine whether it



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should allow the regulation to lapse, prolong its duration or revise it to take into account new market developments such as the increased importance of online sales and the emergence of new market players e.g. online platforms, brought to light in its May 2017 e-commerce inquiry report and by the case-law of the Court of Justice.

Regulation No 316/2014 on technology transfer agreements<sup>8</sup> is also directly inspired by the economic approach. Exemption is subject to the absence of a market share exceeding a pre-determined threshold - 20 or 30% according to the case, as long as the agreement is free of hardcore restrictions. The regulation also provides for "red" clauses, which, although they do not put at risk the exemption of the agreement, are not exempted, and for a mechanism for withdrawal and non-application of the benefit of the regulation. Operators welcomed this legislation<sup>9</sup>. Nevertheless, the Commission has faced much criticism for adopting an economic approach considered too biased (due to the inclusion of too many "red" clauses limiting the freedom of operators), and too general and unsuitable for the high-technology sector. Professionals have claimed that the market share threshold could prevent a greater legal certainty in the field, insofar as it is often difficult to precisely ascertain operators' market shares and that they are of little relevance on dynamic and constantly evolving markets<sup>10</sup>. Some have proposed defining the threshold of the safe harbor, following the US guidelines relative to licensing agreements<sup>11</sup>, taking into account the number of independent sources of technology<sup>12</sup>. More fundamentally, economics commentators have been highly critical of the Commission's approach of sacrificing the legitimate protection of intellectual property rights by calling into question the right to transfer them freely by the use of licenses. According to them, the Commission has under-estimated the positive incentive effects of intellectual property rights in the creation and motivation they engender in respect of future inventions and investments and the regulation would inevitably lead to an erosion of the value of those rights, a decrease in transfers in the form of licenses, an inefficient allocation of resources, R&D investments being diverted from Europe to the USA and a general despondency in respect of the effort to make new inventions. In addition, the lack of specialized national courts would render any efficient

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<sup>8</sup> Commission Regulation (EU) No 316/2014 of 21 March 2014 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of technology transfer agreements.

<sup>9</sup> Joint Comments of the American Bar Association's Sections of Antitrust law etc. on the application of the EU regulation: "the proposed reforms constitute a major improvement to the current highly complex and formalistic TTBER, introducing a conceptually sounder, more economics-based approach to the competition law treatment of technology licensing agreements".

<sup>10</sup> ABA Comments, see above, 3.

<sup>11</sup> U.S. Department of Justice and Federal Trade Antitrust Guidelines for the Licensing of Intellectual Property, 1995.

<sup>12</sup> ABA Comments, see above, 3.



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application of the Regulation illusory, as this could only be ensured by a system of notification to a specialized authority.

As a result of the consultations carried out on the draft regulation, the Commission agreed to more flexibility in respect of the hardcore restrictions by granting a wider margin for maneuver to technology holders (whether in respect of the fixing of sale prices to third parties, limiting production or the sharing of markets or customers). On the other hand, it refused to compromise on the market share thresholds defined, arguing that the regulation was not intended to only apply to the high technology sector and that in any case, there was no assumption that the agreement was unlawful due to the non-application of the exemption.



## CHAPTER 3

# EXCLUSIVE DISTRIBUTION

### Section 1 Lawfulness of network

#### II. Restrictive agreements

##### B. Rule of reason

#### 3.16. Free choice of distribution system.

The supplier is free to choose the method of distribution he sees fit, on condition that he does not infringe the competition rules when refusing a candidate reseller. The network promoter can decide on the strategy of development and establishment and may leave a territory free of any representation<sup>13</sup> or have several types of commercial relationships with its distributors coexist, and can, in particular, create only a few exclusive territories provided that there is no discrimination within each category of distributors<sup>14</sup>. He can also change the organization of the distribution network without the distributors having an automatic right to insist on maintaining the status quo<sup>15</sup>. The freedom to organize the network is a basic principle subject to the proviso that the methods of distribution chosen do not have as their object or effect the distortion of the functioning of the market<sup>16</sup>. It is thus open to the supplier to consolidate the distribution of its products and regroup them within a single undertaking without that operation being qualified as an anticompetitive agreement between the producer and the new distributor<sup>17</sup>. The supplier can decide to switch from a selective distribution system to an exclusive distribution<sup>18</sup>, or from an exclusive distribution system to a franchising system<sup>19</sup>: the decision to favor one network over another is not anticompetitive in character<sup>20</sup>. The change should not be done in haste

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<sup>13</sup> TGI Paris, 7 September 2004, LawLex042212: "[the contractor] is free to choose its partner and to leave a territory free of any dealership [...] the strategy for the development of a network of exclusive or specific dealerships concerns the car manufacturer alone, without complaints being levelled against him for the refusal to set up an automobile dealership in a determined geographic sector."

<sup>14</sup> CA Paris, 2 November 2016, LawLex161816.

<sup>15</sup> Competition Council decision No 98-D-32 of 26 May 1998, LawLex023173; See also, for a recent restatement of the principle, Cass. com., 2 December 2008, LawLex082172, confirming "The right for any supplier to modify the organization of its distribution network without its customers having an acquired right to the maintenance of their situation"; CA Paris, 21 January 2009, LawLex091112; CA Paris 3 May 2017, LawLex17823.

<sup>16</sup> Competition Council decision No 04-D-55 of 10 November 2004, LawLex043259.

<sup>17</sup> Competition Council decision No 01-D-42 of 11 September 2001, LawLex023432.

<sup>18</sup> CA Paris, 10 February 1995, LawLex025448.

<sup>19</sup> CA Paris, 16 October 1992, LawLex022640.

<sup>20</sup> Competition Council decision No 06-D-26 of 15 September 2006, LawLex061971.



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or give rise to a sudden or abusive breaking-off of business relations. The distributor must have received adequate notice. Similarly, the supplier is free to establish a system which combines selective and exclusive distribution as long as active and passive sales are permitted and it is within the thresholds laid down by EU law<sup>21</sup>.

In the name of the principle of freedom to organize the network, the supplier may take protective measures by granting aid to distributors who have been appreciably affected by the development of parallel imports, where that aid stimulates competition between network members and non-network distributors<sup>22</sup>. This is the case for a system of commercial aid to dealers whose activity has been affected locally, and appreciably, by the development of parallel imports, when the manufacturer is not in a dominant position on the market at issue, the aid is not intended to restrict the commercial freedom of the recipients, is not granted in a discriminatory manner and contributes to the development of competition<sup>23</sup>.

### Section 2 Resale outside network

#### II. Protecting the network

##### 3.31. Unlawful use of the mark.

Protection of the marker can be through a trade mark infringement action or an action for unfair competition where the use of the mark creates confusion in the minds of consumers.

Article L. 716-9 of the Intellectual Property Code criminally sanctions the infringement arising from the use of a mark without authorization. It has thus been ruled that the use without authorization of a trade mark by an operator who is neither the manufacturer's agent nor distributor constitutes an infringement and is characteristic of manifestly unlawful disruption<sup>24</sup>. This is also the case when the manufacturer's shield has been reproduced as the wallpaper on the website of a third party reseller which is not associated with an offer of sale, nor the provision of any information in respect of vehicles sold<sup>25</sup>,

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<sup>21</sup> Competition Council decision No 03-D-42 of 18 August 2003 relative to practices implemented by Suzuki and others on the motorcycle distribution market, LawLex033459; Article 4 of the Regulation on Vertical Restraints prohibits bans on active and passive sales within a system combining selective and exclusive distribution; confirmed in appeal by CA Paris, 4 May 2004, LawLex04953.

<sup>22</sup> CA Paris, 29 June 2004, LawLex041644.

<sup>23</sup> Competition Council decision No 03-D-66 of 23 December 2003, LawLex0456; No 03-D-67 of 23 December 2003, LawLex0478; confirmed by CA Paris, 29 June 2004, LawLex041644; 12 July 2005, LawLex059786; upheld by Cass. com., 17 January 2006, LawLex06439.

<sup>24</sup> TGI Lyon, 3 October 2001, LawLex024745.

<sup>25</sup> TGI Paris, 20 December 2002, LawLex03837, confirmed CA Paris, 8 September 2004, LawLex043335.



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or using the word "specialist" followed by the trade mark as a domain name without reference to the name of the reseller<sup>26</sup>.

The rule on exhaustion of trade mark rights allows non-network resellers using a supplier's trade mark to sell its goods to avoid infringement claims if they are able to show that the licensor has consented to the commercialization of the goods on the European market (Intellectual Property Code, Art. L. 713-4). The production of invoices which are not contemporaneous with the facts does not allow the reseller to provide evidence that he obtained the stocks from an authorized distributor located in the EEA<sup>27</sup>. The burden of proof of the absence of consent to market the goods within the EEA is reversed where the third party is able to show that the manufacturer prohibits parallel exports and that if he were to bear the burden of proof this would create a real risk of partitioning of national markets<sup>28</sup>. Such is the case where the non-network importer shows that passive sales are *de facto* prohibited within the network<sup>29</sup>. Likewise, a third party sued for the use of a trade mark in a catalog to designate authentic products may rely on the exhaustion of rights where he has faced refusals to sell after having revealed his sources of supply<sup>30</sup>. In contrast, merely establishing that parallel imports would be profitable due to the price differences between Member States<sup>31</sup> or that the rightholder has brought a large number of infringement actions<sup>32</sup>, is not sufficient to demonstrate that trade marks proprietors are blocking them. **The courts are not in agreement as to how recent the evidence needs to be to establish the existence of a risk of foreclosure: whereas for some, to establish the existence of such a risk, the third party reseller must rely on evidence relating to a period that is sufficiently close if not contemporary to the marketing of the goods held in customs and not on facts and court rulings from more than five years before<sup>33</sup>, others believe that even older evidence may be of sufficient probative value if the supplier does not establish that it has changed its practices since that time<sup>34</sup>. The existence of resales between network members and retailers located on other territories, the numbers of which indicate that they are not**

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<sup>26</sup> TGI Paris, 20 December 2002, LawLex03837.

<sup>27</sup> TGI Paris, 15 January 2016, LawLex16209.

<sup>28</sup> ECJ, Case C-244/00 Van Doren + Q [2003] ECR p. I-3051, LawLex054595.

<sup>29</sup> CA Paris, 29 November 2013, LawLex131722; upheld by Cass. com., 10 November 2015, LawLex151443; CA Paris, 15 April 2014, LawLex141898.

<sup>30</sup> Cass. com., 26 February 2008, LawLex08255 rejecting the appeal against CA Caen, 10 January 2006, LawLex08264.

<sup>31</sup> TGI Paris, 15 January 2016, LawLex16209; 8 April 2016, LawLex16844, upheld by CA Paris, 23 January 2018, LawLex18183.

<sup>32</sup> TGI Paris, 8 April 2016, LawLex16844.

<sup>33</sup> TGI Paris, 8 April 2016, LawLex16844, upheld by CA Paris, 23 January 2018, LawLex18183; Contra: CA Paris, 3 February 2017, LawLex17245.

<sup>34</sup> CA Paris, 3 February 2017, LawLex17245; 1 June 2018, LawLex18843.



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merely one-off or very exceptional sales, rules out any claim of a risk of partitioning<sup>35</sup>. Where the third party non-network member is unable to establish the existence of a risk of market partitioning, it must demonstrate that each copy of the allegedly infringing products was put into circulation in the European Economic Area by the proprietor of the trade mark or with his consent<sup>36</sup>. In addition, the rule of exhaustion of rights applies only if the products marketed by the third-party reseller are authentic. In effect, proof of the lack of authenticity of the products sold establishes by itself the lack of consent of the trade mark proprietor to their marketing in the European Economic Area<sup>37</sup>. The courts have been very strict on suppliers on this point and would appear to make the proof of lack of authenticity subject to the establishment of strict and clearly-defined quality control procedures "relating to the specific and invariable characteristics of objective points of verification of the products that come out of the manufacturing plants"<sup>38</sup>.

The use of the trade mark can be the source of unfair competition. Thus, a reseller cannot use as a shop sign the trade mark of a competitor in order to create confusion in the minds of the public as to its status as an exclusive distributor<sup>39</sup>. An exclusive distributor may, even without holding any IP rights over the the brand, can also bring an action in unfair competition against the importer of infringing products, when they are likely to create confusion as to the origin of the marketed products<sup>40</sup>. A former distributor may also be guilty of attempting to create confusion and thus of unfair competition where it continues to allow customers to think that it is still a network member<sup>41</sup>, notably by adopting a similar logo to the official one<sup>42</sup>, by continuing to use the licensor's logo<sup>43</sup>, its advertising billboards<sup>44</sup>, using its trade mark and passing itself off as an authorized agent<sup>45</sup>, or using or refusing to return the distinctive signs indicating network membership<sup>46</sup>. On the other hand, the use by a garage owner and former distributor

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<sup>35</sup> CA Paris, 14 February 2017, LawLex17349. See also, a contrario, CA Douai, 14 January 2015, LawLex1584 and CA Paris, 3 February 2017, LawLex17245, which finds a risk of foreclosure when the retrocessions invoked relate only to quantities that are too low or only constitute ad hoc sales.

<sup>36</sup> CA Paris, 23 January 2018, LawLex18183.

<sup>37</sup> CA Paris, 23 January 2018, LawLex18183; CA Paris, 22 May 2018, LawLex18781.

<sup>38</sup> Cass. com., 10 November 2015, cited above.

<sup>39</sup> CA Toulouse, 19 June 1997, LawLex021248; CA Paris, 8 April 1998, LawLex021138.

<sup>40</sup> CA Paris, 2 February 2016, LawLex16299.

<sup>41</sup> Cass. com., 9 February 1993, LawLex021668; CA Orléans, 26 February 1998, LawLex021172; TGI Vienne, 15 May 2003, LawLex032131.

<sup>42</sup> CA Paris, 1 February 2002, LawLex020555.

<sup>43</sup> CA Dijon, 3 July 1997, LawLex021239: The former dealer who continues to use the logo of the licensor and does not amend its inclusion in the directory, creates a wrongful risk of confusion. See also on inclusion in the directory, Cass. com., 9 June 2004, LawLex041459.

<sup>44</sup> Cass. com., 17 January 1995, LawLex021498.

<sup>45</sup> Cass. com., 15 December 1998, LawLex021034; T. com. Nanterre, 5 November 2004, LawLex043331.

<sup>46</sup> CA Paris, 9 July 1992, LawLex021717; TGI Lyon, 27 January 2004, LawLex04207; TGI Lille, 2 March 2004, LawLex04797.



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of the term "specialist" is only a wrongful act if the undertaking is unable to bring proof of the genuine nature of the description or if it creates confusion with network members<sup>47</sup>.

The use of the mark without authorization is not only a source of confusion but can also characterize free-riding which allows the perpetrator to take advantage of the network's reputation, and, without any disbursement, to profit from the commercial benefits of the latter. A former distributor maintaining a listing as a reseller of new vehicle on an internet search engine<sup>48</sup>, or a former agent using a trade mark<sup>49</sup> is a usurpation of the brands's reputation. Usurpation can also be indirect as is the case where the distributor claims to carry all the spare parts of the brand<sup>50</sup>.

### Section 3 Formation of contract

#### **3.33. Breakdown of negotiations.**

Negotiations often precede the conclusion of contracts and may be spread out over time and differ as to intensity. Although there is a principle of freedom of termination of negotiations, abuse committed while exercising that freedom is likely to incur the tort liability of its perpetrator. For such purpose, the victim must establish the existence of misconduct, harm and a causal link in accordance with the provisions of Articles 1240 and 1241 (formerly 1382 and 1383) of the Civil Code. Only the circumstances of the termination are likely to constitute misconduct and not the mere fact of terminating the negotiations<sup>51</sup>.

The suddenness of the termination may justify the awarding of damages, particularly by reason of the costs incurred by the victim during negotiations<sup>52</sup>. **The loss stemming from the premature termination of the negotiations for the conclusion of an exclusive distribution contract cannot include the expected returns from the implementation of the contract or the loss of a chance to obtain those revenues, in the absence of any certainty as to the success of the negotiations**<sup>53</sup>. However, suddenness is excluded where the negotiations have lasted for more than a year<sup>54</sup>, without the candidate submitting the documents

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<sup>47</sup> Cass. com., 17 December 1991, LawLex021768; CA Rouen, 4 September 1997, LawLex021231, use by non authorized dealer of the term "specialist" of the brand with the intention of leading customers to believe in its membership to the network; Cass. com., 13 January 1998, LawLex021194, advertisements presenting a repairer as a specialist of a brand.

<sup>48</sup> TGI Vienne, 15 May 2003, LawLex032131, on the use of the trade mark in association with the terms "supplier" and "new cars".

<sup>49</sup> Cass. com., 29 June 1993, LawLex021632.

<sup>50</sup> CA Bordeaux, 2 June 1997, LawLex021254.

<sup>51</sup> Annual report of the Cass. com. for 2006, La Documentation française, 2007, 400.

<sup>52</sup> Cass. com., 20 November 2007, LawLex10455.

<sup>53</sup> Cass. com., 26 April 2017, LawLex17809.

<sup>54</sup> CA Versailles, 6 November 1997, LawLex025061.



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required by the supplier<sup>55</sup>. The fact of giving a mandatory character to the time-period during which negotiations must be conducted does not give the termination an abusive character<sup>56</sup>. The termination of negotiations may be due to the qualities of the candidate for exclusive distribution who does not meet the conditions laid down by the supplier<sup>57</sup> or its dilatory conduct<sup>58</sup>. By contrast, the supplier incurs liability when its conduct is flippant<sup>59</sup> or when it purports to rely on a breach on which the termination of the previous contract was based<sup>60</sup>.

Although the termination of negotiations may result in the loss of opportunity to reconvert, the victim must however bring evidence of the feasibility of the reconversion<sup>61</sup>.

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<sup>55</sup> CA Paris, 10 November 1995, LawLex025508.

<sup>56</sup> CA Paris, 28 June 1995, LawLex025478.

<sup>57</sup> CA Paris, 28 June 1995, LawLex025479, approved by Cass. com., 6 January 1998, LawLex025084; CA Paris, 15 November 1996, LawLex025616: the termination of negotiations that should have resulted in the conclusion of a new exclusive distribution contract is attributable to the distributor only where the latter refuses to comply with the conditions set forth by the supplier.

<sup>58</sup> CA Paris, 29 September 2000, LawLex024776.

<sup>59</sup> T. com. Bobigny, 18 December 1997, LawLex025082.

<sup>60</sup> CA Paris, 5 July 2017, LawLex171259.

<sup>61</sup> Cass. com., 20 November 2007, LawLex10455.



## Section 4 Performance of contrat

### **I. Supplier's rights and obligations**

#### A. Supplier's rights

#### **3.37. Unilateral fixing and inviolability of price.**

The supplier may unilaterally fix the prices of the contract goods where the use of that prerogative is non-abusive. The price of the goods is generally fixed by reference to the prices in the supplier's catalog or to the market price<sup>62</sup>. There would appear to be nothing preventing a unilateral change in the price by the supplier during performance<sup>63</sup>.

As a test for abuse, the Plenary Assembly based itself, in the judgments of 1995, on Articles 1134 and 1135 (now Articles 1104 and 1194) of the Civil Code, which enabled it to use the good faith obligation. The assessment of the abuse may be carried out according to two criteria: objective or subjective. An objective analysis is similar to an economic approach of the distributor/supplier relation, whereas the subjective analysis only relates to the events of the contractual relation. These apparently contradictory approaches are in fact complementary.

Where the court is assessing the abuse, it compares the price charged by the supplier with the market price. In this mitigated version of "injury", the price is held abusive where it significantly exceeds prices usually charged. To determine the average price, account must be taken of price fixing objective elements, such as product quality, reputation of the brand, supplier's assistance, significance of advertising campaigns etc. Thus, there is neither abuse in the fixing of the price, nor "potestativity" where that price is fixed by reference to the supplier's price list by taking account of the cost price of the goods<sup>64</sup>. This competitive price approach presupposes that a reference market exists which relies on precise and verifiable economic data. However, where the gap between the market price and the price required by the distributor is an indication of abuse, it does not constitute the absolute evidence thereof<sup>65</sup>. A supplier's misconduct must be at the origin of this imbalance. **According to the Paris Court of Appeal, the price of the goods as set by the supplier can only reflect the existence of abuse if it is manifestly disproportionate such as to constitute a source of imbalance to the equilibrium of the contract**<sup>66</sup>.

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<sup>62</sup> CA Paris, 5 April 1996, LawLex025561; CA Orléans, 22 October 1996, LawLex025608; Cass. com., 26 January 1999, LawLex025175.

<sup>63</sup> Cass. com., 11 June 1996, LawLex025575.

<sup>64</sup> Cass. com., 26 January 1999, LawLex025175.

<sup>65</sup> CA Paris, 27 June 1997, LawLex025029.

<sup>66</sup> CA Paris, 8 March 2017, LawLex17474.



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From a subjective point of view, the abuse consists in a misconduct committed during the performance of the contract. It must be retained each time the supplier fixes the prices in its own interest to the detriment of the co-contracting party and in contradiction with the initial forecasts. The intention to cause harm is however not required<sup>67</sup>. Accordingly, if the price is freely negotiated by the parties under the laws of supply and demand, there is no abuse in the absence of dominant position and arbitrary conduct from the supplier<sup>68</sup>. The distributor cannot blame the supplier for an unfair price policy which prevents him/her from achieving a sufficient margin, where the supplier has granted 60% discount on the public price (exclusive of taxes) of items in its collection and offered to provide 2,000 free catalogues and to participate in its advertising and operating costs<sup>69</sup>. Nor can he claim to be forced to accept all price changes decided by the supplier where the contract provides for the possibility to terminate subject to compliance with a notice period<sup>70</sup>.

The burden of proof of the abuse is on the distributor who claims to be a victim thereof<sup>71</sup>. Although that proof may be brought by any means, an expert assessment is generally necessary insofar as the abuse relies on precise economic criteria.

Since 1995, the possibility for suppliers to unilaterally fix prices recognized by the Court of Cassation has not raised any major difficulty. Cases of abuse have proved to be very rare in practice. This balance has however recently been called into question by the interpretation by the public authorities of the Hamon Law of 17 March 2014. The new mandatory single commercial agreement between suppliers and distributors must specify which obligations the parties must respect in order to fix the price at the end of commercial negotiations, in particular the initial price scale, the terms of the transaction resulting from the negotiation, price reductions, commercial cooperation and the "distinct services". Those factors contribute to the determination of the price and enter into force concomitantly with the price agreed upon, no later than March 1 of each year. Article L. 442-6, I, 12° of the Commercial Code introduced by the Hamon Law establishes a regime of liability and civil fines which sanctions the placing, settling or invoicing at a price different from the agreed price resulting from the application of the price scale set out in the general terms of sale accepted by the buyer or the price agreed upon in the commercial

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<sup>67</sup> Cass. com., 29 November 1994, No 91-21.009; CA Paris, 31 March 1995.

<sup>68</sup> Cass. com., 21 January 1997, LawLex025629.

<sup>69</sup> CA Paris, 21 June 2002, LawLex043317.

<sup>70</sup> CA Montpellier, 1 July 2014, LawLex142289

<sup>71</sup> Cass. com., 28 November 2000, LawLex024375: the abuse of right in the fixing of the price of goods supplied to the dealer must be established by the one who claims it.



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negotiation resulting in the single commercial agreement as amended where appropriate by a rider or re-negotiation between the parties.

According to an information notice issued by the DGCCRF, as a result of all those factors the supplier can only increase prices during the course of the year "subject to the consent of the other party, materialized by a rider to the contract", and the price can only "change in the course of the contract by agreement between the two parties"<sup>72</sup>.

The public authorities do accept however that "in sectors where supplier prices frequently change during the performance of the contract, the parties may provide from the outset in the single commercial agreement, for the principle and the practical modalities of the acceptance by the customer of each proposal of price change by the supplier".

This does not however take away from the fact that for the authorities, prices are fixed and intangible for one year, and that in all cases any change requires the formal acceptance of the other party by a rider which, in addition, should not undermine the economic balance of the contract<sup>73</sup>.

In other words, according to the public authorities, French law has laid down a principle of price rigidity with fixed prices and their inviolability for one year for the products subject, under ordinary law, to the single commercial agreement. The annual freezing of prices thus recommended is however neither economically viable nor does it have any legal basis.

Even in the short term, in a market economy, suppliers prices will vary regularly over the course of the year. An economic study has shown that nearly 50% of companies change their prices more than once over the course of a normal year, 7.5% between 4 and 12 times, 4.3% between 12 and 52 times, 8.6% between 52 and 365 times and 1.6% more than 365 times per year<sup>74</sup>.

To require that all suppliers doing business with distributors maintain a total freeze for one year, unless distributors formally agree to proposed increases, exposes suppliers to significant losses in the event of cost increases or exchange rate variations.

Not only is such a rule non economically sustainable, it also has no real legal basis. In effect, no provision of the Hamon Law imposes an intangible fixed price for a year. The single commercial agreement only

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<sup>72</sup> DGCCRF Information Notice No 2014-185 of 22 October 2014, annulling the first notice on the Hamon Law No 2014-14 of 6 August 2014.

<sup>73</sup> Footnote page 10 of Information Notice of 22 October 2014, 32.

<sup>74</sup> See Table 4.1, BLINDER, *Sticky Prices: Academic Themes Meet The Real World*, in MANKIW (ed.), *Monetary Policy*, University of Chicago Press, 1999, 117-154.



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requires justification of the negotiation of the price. Where the single commercial agreement stipulates that price mentioned may be modified by the supplier under the rules of the civil code, there is no infringement of Articles L. 441-7 or L. 442-6-I-12° in the absence of an inviolable fixed price throughout the year.

The contra legem interpretation of the Hamon Law by the Circular of 22 October 2014 not only opposes the supplier's possibility to modify the price in the course of the year as laid down by the Court of Cassation in its judgments of Plenary Assembly rulings of 1 December 1995, but also clashes with other rules: the rules on restrictive practices recognize that the imposition by one party on the other of an inviolable sale price - when its costs are liable to increase - may constitute the subjecting of a trading partner to an imbalanced obligation<sup>75</sup>.

### B. Supplier's obligations

#### 1° Exclusivity

### **3.47. Internet distribution by the network developer.**

The network leader will naturally be encouraged to develop a website for the purpose of presenting and offering its products for sale. Does the creation and operation of such a site violate the exclusivity granted to the exclusive distributor on its territory?

A landmark decision was rendered in this respect regarding a franchise agreement, but the solution may be transposed to exclusive distribution. In the Flora Partner case, a franchise agreement provided: "territorial exclusivity implies that the franchiser has undertaken for the duration of the contract not to authorize the opening of other sales outlets [bearing the franchiser's business sign] in the exclusive territory, with the exception of the franchisee's sales outlet". A franchisee dissatisfied with the sales achieved with customers domiciled on its territory, from the franchisor's internet site, had successfully sued for violation of the exclusivity<sup>76</sup>. Quashing the decision of the Court of Appeal, the Court of Cassation ruled that "the contract taken out by the parties was only guaranteeing territorial exclusivity to the franchisee in a defined sector and the creation of a website cannot be assimilated to the setting-up of a sales outlet in the protected area"<sup>77</sup>.

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<sup>75</sup> T. com. Lille, 7 September 2011, LawLex111426; upheld by CA Paris, 11 September 2013, LawLex131296; T. com. Meaux, 24 January 2012, LawLex12137, upheld by CA Paris, 4 July 2013, LawLex131139.

<sup>76</sup> CA Bordeaux, 26 February 2005, LawLex04750.

<sup>77</sup> Cass. com., 14 March 2006, LawLex06857, and CA Toulouse, 11 December 2007.



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In any event, where the supplier is entitled to sell products in any area of the French or European territory especially through its own distribution branches or subsidiaries, it should not be criticized for passive sales from a website since the ban on passive sales would then lead to the granting of absolute territorial protection to the distributor and would violate both EU and national competition rules<sup>78</sup>. **The supplier must nonetheless abstain, under penalty of being held liable for unfair behavior, from price-cutting practices on its own website<sup>79</sup>.**

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<sup>78</sup> Commission Notice 2010/C 130/01, Guidelines on Vertical Restraints, OJEU C 130 of 19.5.2010, 1.

<sup>79</sup> CA Paris, 21 March 2018, LawLex18538.



## Section 5 Termination of contract

### **I. Extraordinary termination**

#### B. Conditions of implementation

##### 2° Formal conditions

#### **3.84. Prior formal notice and possibility of derogation from terms of termination clause.**

The ordinance for the reform of contract law has significantly modified the provisions relative to the implementation of termination clauses. Like before, the parties freely set the terms and conditions of the termination. However, new Article 1225 of the Civil Code lays down three formal requirements: the termination clause must specify which commitments, if breached, will result in the termination of the contract; this is subject to the failure to comply with the demands made in the formal demand letter if the parties have not agreed that the contract may be terminated immediately for non-performance; the formal demand letter must, in order to produce its effect, expressly refer to the termination clause. As long as the termination clause is implemented under the conditions provided for in the contract, the termination cannot be abusive<sup>80</sup> as long as it is in respect of a serious breach of obligations<sup>81</sup>. According to new Article 1226, paragraph 4, the burden of proof of the gravity of the breach giving rise to the termination falls to the beneficiary of the obligation. Two cases must however be distinguished.

Where the termination clause provides for an automatic termination at any time, which it may expressly pursuant to new Article 1225, paragraph 2, no prior notification is required<sup>82</sup>. Formerly, if the non-performance concerned an obligation to refrain from doing something, under the provisions of Article 1145 of the Civil Code a formal notice was not necessary to establish non-performance<sup>83</sup>. This rule has been overturned by the new reform: Article 1231 now provides that unless the failure to perform the contract is definitive, damages are payable only if the party in breach first receives a formal demand enjoining him/her to act within a reasonable period of time, without making a distinction between obligations to act and other types of obligations.

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<sup>80</sup> Cass. com., 26 March 2002, LawLex024656.

<sup>81</sup> Cass. com., 9 July 2013, LawLex131101 and 25 September 2007, LawLex071509.

<sup>82</sup> CA Paris, 8 March 1996, LawLex025549: a termination clause for outstanding payments is validly implemented without prior summons of the dealer where it includes a conventional exemption from that formality; Cass. com., 2 March 1999, LawLex025186: the implementation of a clause enabling a termination which is "automatic, at any time" in case of outstanding payments is not subject to prior formal notice to the dealer.

<sup>83</sup> CA Paris, 29 May 1992.



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In the event that the termination clause imposes on the parties a prior formal notice obligation, the implementation of the clause without such notification has been held in the past to be a sudden termination<sup>84</sup>. Subsequently, the commercial chamber of the Court of Cassation has accepted that in the event of a serious breach preventing any continuation of the relationship, the gravity of the conduct of one party can justify the unilateral termination by the other party at their own risk despite of the existence of a termination clause and its terms<sup>85</sup>. Under the reformed Civil Code, this solution is only partially accepted. Although new Article 1226 expressly reserves to the beneficiary of the obligation the possibility to terminate the contract by way of formal notice at its own risk, this option, except in cases of urgency, is subject to the obligation to first enjoin the other party to fulfill the obligations at issue within a reasonable period of time. On the other hand, it does not seem to rule out the possibility of terminating the contract at its own risk for causes other than those laid down in the contract and according to terms other than those related to the observance of a prior formal notice obligation. This remedy, although realistic, has however been contradicted by a stricter ruling of the third civil chamber of the Court of Cassation, which held that the termination clause is binding on the parties and constitutes a waiver by them to the right to unilaterally terminate the contract in the event of a serious breach<sup>86</sup>. Given this contradiction in the case law, operators should ensure they respect the conditions of form and substance of the termination clauses and only resort to the possibility of unilaterally terminating a distribution contract for a serious breach by the other party if the conditions of the termination clause are not perfectly satisfied in case of absolute necessity<sup>87</sup> and be aware of the legal risks they may face. **A recent decision thus held that the termination of a contract without meeting the requirements of the termination clause, which stipulate prior notice, was unreasonable since it was not based on a sufficiently serious breach<sup>88</sup>.** In the drafting of contracts, it is also important to include a general termination clause for serious breaches and more detailed clauses which, because they are non-exhaustive, do not affect the general right to immediately terminate for other serious breaches. Such caution is especially needed because there is an abundance of case law in the field of distribution law where the courts have been particularly strict for contract terminations on the basis of such clauses. **Firstly, a contract cannot be terminated by e-mail when it stipulates that it can only be terminated after**

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<sup>84</sup> T. com. Paris, 22 February 1999, LawLex024731; CA Paris, 20 April 2000, LawLex024774; 17 October 2001, LawLex043464.

<sup>85</sup> Cass. com., 4 February 2004, LawLex10956; 10 February 2009, No 08-415; 1 October 2013, No 12-20.830; Cf., Cass. I<sup>re</sup> civ., 24 September 2009, No 08-14.524.

<sup>86</sup> Cass. com., 9 October 2013, No 12-23.379.

<sup>87</sup> CA Versailles, 20 October 2015, No 14-06812, *Alès Poids Lourds v Mercedes Benz France*, LawLex 20151321: an authorized repairer contract may be terminated without the sending of a formal notice even if the contract requires it, when it is not materially possible to remedy the alleged breach.

<sup>88</sup> CA Paris, 16 May 2018, LawLex18743.&#10;



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the sending of a formal notice letter by express delivery, not heeded within a period of thirty days, in the event of a violation of one of its essential terms<sup>89</sup>. It was subsequently held that where a termination clause imposes a letter of formal notice, that notice must clearly order the distributor to comply with its contractual commitments<sup>90</sup>. This is the case where, in the letter preceding the formal notification, the supplier queries the decrease in sales and describes the distributor's conduct as a breach of contract<sup>91</sup>. This is not the case however where the supplier's formal notice letter does not make any specific complaint against the distributor<sup>92</sup> or does not specify that the failure to pay on the due date will result in the termination of relations<sup>93</sup>. The performance of contractual obligations within the time-period fixed by the letter suspends the effects of the termination clause<sup>94</sup>. Failing such performance, the creditor states that the contract is terminated<sup>95</sup>. Indeed, the termination will take effect as of right when the supplier has sent a formal notice letter by registered mail enjoining the distributor to comply with his exclusivity obligation, and where on expiry of the contractual one-month period the distributor has failed to comply with the demand and has not contested the breach levelled against him<sup>96</sup>

### IV. Sudden termination of established commercial relationship

#### 3.105. Conditions of application.

Article L. 442-6, I, 5° of the Commercial Code sanctions the sudden termination, even if only partial, of an established commercial relationship without sufficient written notice. Initially conceived to tackle the practice of abusive de-listing by certain distributors, the provision is worded in such broad terms that it has been extended to almost all traders for the entire duration of the relationship and even covers the non-renewal of fixed-term contracts. The provision also applies to exclusive distribution agreements. In many cases the courts have found that changes to the distributor's exclusivity arrangement accompanied by considerable price increases by the supplier constitute at least a partial termination of the commercial relationship<sup>97</sup>. Although the courts recognize the supplier's right to change the

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<sup>89</sup> CA Paris, 8 March 2017, LawLex17474.

<sup>90</sup> CA Paris, 20 April 2000, LawLex024774.

<sup>91</sup> Cass. com., 17 January 1995, LawLex021498.

<sup>92</sup> CA Paris, 4 October 2012, LawLex122107.

<sup>93</sup> TGI Paris, 30 November 2004, LawLex053793.

<sup>94</sup> Cass. com., 17 December 1991 (leasing).

<sup>95</sup> Cass. com., 17 January 1995, LawLex021498.

<sup>96</sup> CA Rennes, 14 December 2012, LawLex138.

<sup>97</sup> CA Paris, 6 May 2015, LawLex15570: moving from exclusive to selective distribution; CA Paris, 13 May 2015, LawLex15631, withdrawal of exclusivity granted to two distributors for the direct sale of the contract goods; CA Paris, 13 May 2015, LawLex15599: takeover of distribution by a subsidiary of the supplier with higher prices and harsher commercial terms demanded of the former exclusive distributor. Also see Cass. com., 23 October 2012, LawLex122245.



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organization of its distribution network and to have various categories of distributors coexisting within it, the supplier is required to give its trading partner sufficient advance notice thereof<sup>98</sup>. The courts have also ruled that the non-renewal of a fixed-term exclusive distribution contract which has been extended or renewed several times over a 21-year period, incurs the liability of the supplier granting the exclusivity on the basis of Article L. 442-6, I, 5<sup>o</sup><sup>99</sup>. Likewise, a fixed-term exclusive distribution agreement which, further to a succession of renewals over a period of 18 years, has become an open-ended agreement cannot be terminated with a notice period of less than one year<sup>100</sup>. On the other hand, it has been held that a renewal of a fixed-term distribution agreement on two occasions which expressly excludes any tacit renewal prevents the distributor from relying on the existence of an established commercial relationship due to the risk of non-renewal at the term of each contract<sup>101</sup>. Similarly, the non-renewal at its maturity of a single distribution agreement is not regarded as a sudden termination of an established commercial relationship<sup>102</sup>.

In all cases the notice period granted must be reasonable. Where the relations continued for nineteen years, the distributor is bound by a purchase exclusivity and the products enjoy a certain notoriety, a contractual notice period of eight months is not sufficient and must be increased to twelve months<sup>103</sup>. A notice period of six months is thus regarded as reasonable even though relations had endured over a long period of time, where this is sufficient to allow the multi-brand dealer to overcome the loss of the supplier's products<sup>104</sup> or where the supplier's products only represent 13% of the multi-brand dealer's turnover and where there are no brand-related investments still to be recouped<sup>105</sup>. Further, although the termination notice must take into account the dependence of the victim<sup>106</sup> and investments made<sup>107</sup>, this is not so when the distributor has been relieved of his exclusivity obligation in the course of the notice period and the investments made, even if recent, are of benefit to his other ongoing and future

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<sup>98</sup> CA Paris, 21 March 2018, LawLex18538.

<sup>99</sup> CA Paris, 29 November 2007, LawLex082226.

<sup>100</sup> CA Versailles, 14 October 2004, LawLex053779.

<sup>101</sup> CA Paris, 29 May 2008, LawLex082248.CA

<sup>102</sup> CA Paris, 24 May 2017, LawLex17916.

<sup>103</sup> Cass. com., 12 April 2016, LawLex16816.

<sup>104</sup> Cass. com., 31 January 2006, LawLex06620; CA Paris, 19 March 2014, LawLex141705; see also CA Paris, 8 October 2014, LawLex141054

<sup>105</sup> CA Paris, 19 March 2014, LawLex141705.

<sup>106</sup> CA Paris, 8 February 2017, LawLex17298, finding that the purchase exclusivity imposed on a distributor in consideration of its territorial exclusivity does not place it in a state of dependence when, given the presence of other well-known manufacturers on the market, it does not prevent the distributor from diversifying by selling other products not covered by the clause, including in same specialty.

<sup>107</sup> CA Paris, 8 February 2017, LawLex17298, considering that, in assessing the sudden nature of the termination, account may not be taken of investments made, before such investments had even been requested by the partner, not by the distributor itself but by a Société Civile Immobilière in which the Chairman of its Board of Directors holds an interest.



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activities<sup>108</sup>. The fact that there is a contractual notice period does not deprive the court of its discretion: the contractual notice period will only be enforced if it is deemed sufficient having regard to the length of the contractual relationship between the parties<sup>109</sup>. Thus, the granting of one month's notice as provided for in the contract is not insufficient where the termination came about due to a breach by the dealer which itself would have justified an immediate termination<sup>110</sup>. Controversially, some judgments have held that the notice period granted to a distributor who is the victim of the termination of an established commercial relationship is doubled where the products in question bear the manufacturer's brand<sup>111</sup>. But this doubling of the notice period in principle only applies to suppliers manufacturing products according to the specifications of the distributors who are proprietors of the trade mark<sup>112</sup>. **The Court of Cassation therefore intervened to clarify that the doubling of the notice is not justified in this case<sup>113</sup>. Furthermore the Court of Cassation considers that a letter sent after the notification of the termination, in which the supplier offers to extend the notice period initially granted, may not be taken into consideration when assessing the reasonable nature of that initial notice period<sup>114</sup>.**

Lastly, the notice period granted must be real and orders placed during that period must be fully met unless they are unusual vis-à-vis the stocks still in the possession of the distributor<sup>115</sup>. **Canvassing the distributor's customers in the course of the notice period also incurs the liability of the supplier<sup>116</sup>, provided however that the marketed products are covered by the exclusivity clause<sup>117</sup>. Likewise, the withdrawal of exclusivity during the notice period removes the benefit of the notice as the distributor can no longer rely on the exclusivity to reorient the business<sup>118</sup>, unless he is paid a commission on sales made by third parties on his territory<sup>119</sup> or the waiver of the exclusivity is mutual<sup>120</sup>. On the other hand, the distributor's refusal to continue to perform its contractual obligations during the notice period does not characterize a sudden termination of established commercial relations when the notice offered includes a substantial change in the contractual terms and conditions<sup>121</sup>.**

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<sup>108</sup> CA Paris, 13 January 2016, LawLex1671, upheld by Cass. com., 11 May 2017, LawLex17882.

<sup>109</sup> CA Reims, 4 April 2011, LawLex11782; CA Colmar, 16 January 2013, LawLex13105; CA Paris, 5 November 2014, LawLex141242.

<sup>110</sup> CA Poitiers, 11 January 2011, LawLex11114.

<sup>111</sup> CA Reims, 4 April 2011, LawLex11782. For a contrary judgment see CA Nancy, 29 October 2014, LawLex141221.

<sup>112</sup> CA Nancy, 29 October 2014, LawLex141221.

<sup>113</sup> Cass. com., 6 September 2016, LawLex161419.

<sup>114</sup> Cass. com., 5 April 2018, LawLex18569.

<sup>115</sup> CA Paris, 8 October 2014, LawLex141054; CA Paris, 25 February 2015, LawLex15249.

<sup>116</sup> CA Paris, 8 February 2017, LawLex17306; 19 April 2017, LawLex17737.

<sup>117</sup> CA Paris, 17 January 2018, LawLex18114.

<sup>118</sup> Cass. com., 10 February 2015, LawLex15184.

<sup>119</sup> CA Paris, 10 February 2016, LawLex16368.

<sup>120</sup> CA Paris, 13 June 2018, LawLex18929.

<sup>121</sup> CA Paris, 16 May 2018, LawLex18757.



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Breaches by the distributor of his contractual obligations may nevertheless justify termination of the contract without notice. To do so the supplier must show that the breach is of a sufficient degree of seriousness<sup>122</sup>: failing to place orders<sup>123</sup> or make sales<sup>124</sup> over a long period characterize a serious breach of the distributor's contractual obligations and justify an immediate termination; termination for failure to meet sales targets is, on the other hand, a more controversial issue<sup>125</sup>, **the Court of Cassation considering that it does not constitute a serious enough breach to justify an immediate termination of commercial relations, even in the presence of a termination clause stipulating otherwise<sup>126</sup>**. Similarly, a mere late payment has been held insufficient to justify an immediate termination<sup>127</sup> **especially when the amounts at issue are insignificant<sup>128</sup>**. The seriousness can result from the repeated nature of the breaches or the fact that the behavior denounced was not modified after the partner was issued a warning. Reproaches which were mentioned neither in the course of performance of the contract nor in the termination letter cannot be invoked to justify the supplier's decision<sup>129</sup>. A serious breach makes the pursuit of relations impossible to maintain; thus, the supplier who does not terminate the contract immediately but notifies his partner of its non-renewal on expiry cannot subsequently claim a serious breach to justify the decision not to renew<sup>130</sup>. Where the partners are in business with regard to two different activities, a breach in relation to one of them cannot be relied upon in order to terminate relations in respect of the other<sup>131</sup>. However, if the distribution agreement provides that serious breaches give rise to its immediate termination and that, if they are of such a nature as to affect the relations of trust and partnership between the parties, all contracts between them may be terminated under the same terms, it has been held that serious breaches committed in the performance of a concession contract leading to the deterioration of the image of the brand justified the termination of the authorized repairer contract<sup>132</sup>.

The excesses, which in some cases the imposition of long notice periods for the termination of established commercial relations have created, have given rise to criticism by legal commentators and

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<sup>122</sup> CA Nancy, 29 October 2014, LawLex141221, termination for breach that is not described in the contract as a clearly established breach of one of its essential terms held to be contrary to Article L. 442-6.

<sup>123</sup> CA Paris, 1 July 2009, LawLex093591.

<sup>124</sup> CA Paris, 16 January 2017, LawLex17146.

<sup>125</sup> Cass. com., 31 January 2006, LawLex06620, finding non-performance; CA Lyon, 13 January 2011, LawLex11317 and CA Reims, 4 April 2011, LawLex11782, no serious breach ("faute grave"); Cass. com., 9 July 2013, LawLex131101.

<sup>126</sup> Cass. com., 5 April 2018, LawLex18568 and previously Cass. com., 9 July 2013, LawLex131101.

<sup>127</sup> CA Nîmes, 24 January 2013, LawLex13117.

<sup>128</sup> CA Paris, 19 April 2017, LawLex17737.

<sup>129</sup> CA Paris, 4 July 2018, LawLex181037.

<sup>130</sup> CA Paris, 4 juillet 2018, LawLex181037.

<sup>131</sup> CA Amiens, 11 October 2012, LawLex122177.

<sup>132</sup> Cass. com., 10 February 2015, LawLex15371.



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caused the courts to find ways of circumventing the scope of application of the rule. Furthermore, the constitutional nature of the rule and its conditions of application as well as its compliance with EU competition law are all debatable.

In view of the fact that the "Conseil constitutionnel" has enshrined the constitutional concept of the freedom to unilaterally terminate a private law contract of indefinite duration at any time<sup>133</sup>, is the requirement of excessively long notice periods - sometimes also including a termination indemnity - not contrary to that constitutional right? As the failure to comply with the notice period is punished by a civil fine of up to EUR 2 million, do the lack of foreseeability of the frequently random length of notice granted and the unclear nature of the scope of the rule not violate the principle of the legality of criminal offenses and penalties as guaranteed by the Declaration of the Rights of Man and of the Citizen of 1789?

There is no doubt that the courts will continue to face problems arising from the question of what is and what are the conditions of application of an established commercial relationship. Legal commentators have been even more radical in their criticism of the most frequent cases in which there is no sector-wide agreement laying down minimum notice periods: is it not the case that the use of the conjunction "and" in Article L. 442-6, I, 5° of the Commercial Code requires the existence of such agreements? The courts currently think not.

The courts have recognized the incompatibility of an excessive application of the rule on notice periods with EU law. With regard to motor vehicle distribution, agreements meeting a certain number of conditions were, until 2013, fully exempt from the application of the rules on restrictive agreements. They included the requirement to comply with at least two years' notice for ordinary terminations or one year for terminations for network reorganizations. But, in order to justify the implementation of the autonomous discretion of the Minister of the Economy laid down in Article L. 442-6 of the Commercial Code, the French courts have ruled that that provision met the aim of "preserving the economic public order"<sup>134</sup>. How can a rule of domestic French law which pursues the same objective as an EU competition rule challenge a notice period held to be valid under European law? In five judgments handed down on 11 May 2011, the Paris Court of Appeal ruled on that basis in favor of a supplier claiming that the one-year notice period granted for network reorganization in conformity with the motor vehicle block exemption regulation could not be invalidated by a provision of national competition

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<sup>133</sup> Constitutional Council, 9 November 1999, No 99-419 DC.

<sup>134</sup> Cass. com., 8 July 2008, LawLex081091.



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law<sup>135</sup>. The courts of appeal in Limoges and Versailles on the contrary ruled that the notice periods laid down in Regulation No 1400/2002 cannot serve as a reference for the assessment of the minimum notice due to the victim of a sudden termination of an established commercial relationship<sup>136</sup>, although the rationale given in those judgments is not particularly convincing and is totally incompatible with the principle of the primacy of EU law. The Court of Appeal in Paris has more recently rejected the argument of the incompatibility of Article L. 442-6 of the Commercial Code with competition law on the basis of more solid reasoning. It held that compliance with the two-year period pursuant to Regulation No 1400/2002 does not preclude the need to review its conformity with Article L. 442-6, I, 5° of the Commercial Code insofar as the two texts do not pursue the same aims<sup>137</sup>. In other words, Article L. 442-6, I, 5° of the Commercial Code aims to protect the terminated party and is part of the public policy of protection of the weaker party [*ordre public de protection*] whereas European competition law would fall under public policy provisions in the general interest [*ordre public de direction*]. This analysis is, however, in total contradiction with the jurisprudence of the Constitutional Council<sup>138</sup>, the European Court of Human Rights and the Court of Cassation which have upheld the prerogatives of the Minister of the Economy in implementing Article L. 442-6, I, 5° of the Commercial Code for the protection of "public policy" [*ordre public*] and "the defense of a general interest", it being specified that "the Minister acts above all in defense of economic public policy which is not restricted to the immediate interests of suppliers"<sup>139</sup> and for the protection of the market<sup>140</sup>.

The higher courts consider that Article L. 442-6, I, 5° is part of public policy provisions in the general interest and that its aim is the protection of competition. It is therefore not possible to limit the scope of this provision to the protection of competitors in order to circumvent the principle of primacy. This fundamental contradiction needs to be addressed rapidly and the subject of a referral for preliminary ruling to the European Court of Justice. The law in France as it stands is currently incoherent.

### **3.106. Sanction for insufficient notice.**

Where the notice granted is insufficient, the victim of the termination may bring an action demanding the pursuit of the relationship, subject to periodic penalty payment for non-compliance, or, as is more often the case, to compensation for the harm suffered. Traditionally, if the claimant was able to find a

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<sup>135</sup> See especially CA Paris, 11 May 2011, LawLex11946.

<sup>136</sup> CA Limoges, 9 February 2012, LawLex12294; CA Versailles, 4 September 2012, LawLex122118.

<sup>137</sup> CA Paris, 24 June 2015, No 13-05110, LawLex15837.

<sup>138</sup> Constitutional Council, No 2011-126 QPC of 13 May 2011.

<sup>139</sup> ECHR, 17 January 2012, No 51255108.

<sup>140</sup> Cass. com., 8 July 2008, LawLex081091.



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new supplier during the notice period, the trial courts would reduce the required notice period or even conclude that no harm had been suffered<sup>141</sup>.

The Court of Cassation now considers that the appropriate notice period should be assessed having regard to the duration of the business relationship and the circumstances prevailing at the time of the notification of termination<sup>142</sup>. The Court has thus held that account should not be taken of events subsequent to the termination such as the distributor switching to other business<sup>143</sup>. It has also stated that "in the case of insufficient notice, the resulting harm is assessed with regard to the duration of notice judged to be necessary". This means that the amount of the loss suffered is evaluated on the day of termination according to the notice that ought to have been granted, even if, due to the fact that the other party has been able to find new business in the meantime, it is not needed. This solution seems questionable. Notice of termination of a contract is intended to give the terminated party the opportunity to find new business; it is not an end in itself but rather a means to achieve that end. Now determining the length of the notice period without ensuring whether that objective has already been achieved lacks coherence. The courts will also sometimes award compensation for loss of profits that would have been made in the months for which notice has not been granted relative to the duration of the notice period as assessed on the day of the termination and without taking account of subsequent events. Such a remedy amounts to awarding an automatic indemnity to a distributor having, as is frequently the case in practice, found a new supplier, for losses that he has not suffered. In such cases, this is no longer "compensation" granted on the basis of liability but a lump sum payment. Such a deviation is cause for concern and would appear unfounded having regard to Article L. 442-6, I, 5° of the Commercial Code which clearly provides for a liability action based on the compensation of the harm suffered, not automatic compensation. The solution is in any case contrary to the principles of civil liability which require an assessment of the injury on the day of the court ruling and not on the day when the event that gave rise to the damage occurred. Not only is it unjust but it also undermines the efficiency of distribution networks by leading to reduced flexibility in contractual relationships which are already subject to too many legal constraints. **The Paris Court of Appeal maintained its opposition to this case law finding it appropriate to take into account the reorganization of the ousted partner when assessing the duration of the notice period<sup>144</sup>. More recently however, it appears to have moved closer to the Court**

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<sup>141</sup> See CA Versailles, 14 February 2012, LawLex12283; CA Rennes, 13 March 2012, LawLex12367; CA Nancy, 3 October 2012, LawLex122189.

<sup>142</sup> Cass. com., 9 July 2013, LawLex131090, quashing CA Rennes, 13 March 2012, LawLex12367.

<sup>143</sup> Cass. com., 6 November 2012, LawLex122304. See also CA Paris, 12 November 2014, LawLex141315.

<sup>144</sup> CA Paris, 28 January 2016 (2 judgments) and 29 January 2016, LawLex16225, LawLex16227 and LawLex16284.



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of Cassation's position in holding that account cannot be taken, to reduce the duration of the notice period, of invoices after the termination which show only that the distributor was able to receive supplies directly from the supplier, for modest amounts, when the order date is not specified<sup>145</sup>, before falling completely into line by excluding the possibility to take account of any post-termination factors<sup>146</sup>. The Court has also held that the fact that the notice period granted by the supplier has allowed the distributor to redevelop its activity does not necessarily mean it is sufficient in light of Article L. 442-6, I, 5° of the Commercial Code<sup>147</sup>.

### VI. International contracts

#### 3.125. Jurisdiction clauses and applicable law in international contracts.

Many exclusive distribution contracts are concluded between foreign suppliers and French distributors. Even in the case where the supplier has a subsidiary in France, it is common for the distribution agreement to be concluded directly between the distributor and the foreign parent company with the subsidiary playing a marketing support and network development role. Such relations are generally formalized in standard agreements allocating jurisdiction to the courts in the supplier's country with the application of the law of that country, but can sometimes be more informal and be based on a series of transactions.

##### 1) Jurisdiction

As a general rule, in disputes relating to contract terminations, French distributors will seek to establish the jurisdiction of the French courts, before which claims are less costly and easier than before foreign courts, and the application of French law, specifically Article L. 442-6 of the Commercial Code. After some hesitation, the French courts will now enforce clauses attributing jurisdiction to foreign courts, including actions based on the termination of established commercial relations which come under tortious liability ("responsabilité délictuelle")<sup>148</sup> as "the tortious nature of the liability incurred [by the party instigating the termination] does not in principle exclude the application of a jurisdiction clause legitimately contracted between the parties"<sup>149</sup>. In international disputes, the courts give a broad interpretation to the scope of jurisdiction clauses, namely by considering that jurisdiction clauses

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<sup>145</sup> CA Paris, 7 February 2018, LawLex18276.

<sup>146</sup> CA Paris, 15 March 2018, LawLex18515.

<sup>147</sup> CA Paris, 4 July 2018, LawLex181042.

<sup>148</sup> Cass. com., 6 February 2007, LawLex07219. For the classification of tortious liability see Cass. com., 6 March 2007, LawLex07349; Cass. Ire civ., 6 March 2007, LawLex07349,

<sup>149</sup> CA Paris, 5 March 2013, LawLex13341; 26 November 2010, LawLex11417.



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purporting to govern all disputes arising from the contractual relationship are sufficiently comprehensive to cover disputes based on the termination of an established commercial relationship<sup>150</sup>.

The enforceability of jurisdiction clauses is systematically challenged unless they are expressly stipulated in the written distribution agreement. By virtue of Article 25 of Regulation No 1215/2012 of 12 December 2012, the clause is only enforceable if it is agreed by both parties, provided that it is in a form which accords with a usage in international trade or commerce of which the parties are or ought to have been aware. The systematic reference, under the postal address of a German company in all its commercial documents, to the competent Munich court<sup>151</sup> or a clause in the general terms of sale printed on the back of an order form<sup>152</sup> were not regarded as jurisdiction clauses as they had not been accepted by the other party. On the other hand, the Court of Cassation has ruled that where a jurisdiction clause is included in the general terms of sale printed on the back of invoices, in an annex to the price list and on the back of order confirmations, the distributor's acceptance is established by the continued payment of the invoices<sup>153</sup>. **This is not the position adopted more recently by the Court of Justice however: in effect it considered that, in the absence of a contract in writing between the parties, a jurisdiction clause set out only in the general terms and conditions of sale listed on the back of the invoices issued by the supplier is not enforceable against the distributor<sup>154</sup>.**

Even when the distributor has agreed to the attribution of jurisdiction to the court of another country, he may also decide to bring a claim for interim relief before the French courts on the basis of Article 35 of Regulation No 1215/2012 (former Article 31 of Regulation No 44/2001) which provides that "[a]pplication may be made to the courts of a Member State for such provisional, including protective, measures as may be available under the law of that State, even if, under this regulation, the courts of another Member State have jurisdiction as to the substance of the matter". The way to circumvent such clauses therefore consists not in bringing a claim for damages but in bringing a claim for interim relief for the continuation of the contract subject to periodic penalty payments for manifestly unlawful disturbance ("trouble manifestement illicite") or for imminent harm. However, the possibility of protective measures being taken assumes that there is a genuine connection between the object of the measures and the jurisdiction of the State of the courts seized, which is not the case where the measures

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<sup>150</sup> Cass. com., 20 March 2012, LawLex12495.

<sup>151</sup> T. com. Pontoise, 2 February 2012, LawLex121949.

<sup>152</sup> Cass. com., 18 January 2011, LawLex1183.

<sup>153</sup> CA Paris, 26 November 2010, LawLex101339, upheld by Cass. com., 20 March 2012, LawLex12495.

<sup>154</sup> CJEU, Case C-64/17 Saey Home & Garden NV/SA, Judgment of 8 March 2018, LawLex18386.



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are essentially to be implemented in another country<sup>155</sup>. Where the claimant is successful in having the jurisdiction clause declared unenforceable or void and brings a claim before the French courts, he will as a general rule be able to impose the application of French law, here Article L. 442-6, I, 5° of the Commercial Code as a mandatory provision of public policy ("loi de police")<sup>156</sup> which supersedes the foreign law<sup>157</sup>. Some exclusive distribution agreements contain asymmetrical choice of court clauses attributing jurisdiction to the place in which the supplier is domiciled whilst at the same time giving the latter the option of choosing the court of the place where the distributor is domiciled and sometimes a completely different competent court. The aim of the option of choice of court to the sole benefit of suppliers is generally to facilitate actions for recovery against distributors, while trying to discourage distributors from bringing liability actions. For a long time the Court of Cassation was very reticent in respect of these asymmetric clauses, initially finding them arbitrary<sup>158</sup>, and later corrected the inadequate legal basis for the beneficiary finding a lack of foreseeability when the latter's discretion was too wide<sup>159</sup>. More recently, it found sufficiently foreseeable an asymmetric clause giving the complainant the discretionary option to choose another jurisdiction<sup>160</sup>. In the same judgement, following the in the Court of Justice's ruling in the Cartel Damages Claims case<sup>161</sup>, the Court of Cassation found that for the jurisdiction clause to apply in cases of claims based on the infringement of competition law, the clause must refer to disputes relating to liability incurred due to anticompetitive practices. These solutions have been subject to much criticism by legal commentators and the debate is probably not yet closed on the matter. Parties are in any event well advised to extensively clarify and define the scope of their jurisdiction clauses in order to ensure their effectiveness.

In the absence of a valid jurisdiction clause, the court competent to rule on the termination of a distribution agreement must be assessed having regard to the criteria laid down in Article 7 of Regulation No 1215/2012 of 12 December 2012. In matters relating to a contract, Article 7 provides that a person

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<sup>155</sup> Cass. com., 20 March 2012, LawLex12495.

<sup>156</sup> For the classification as a mandatory public policy provision, 22 October 2008, LawLex081850.

<sup>157</sup> T. com. Pontoise, 2 February 2012, LawLex121949, LD, April 2012, setting aside the Rome and the Hague Conventions relative to the law applicable to contractual relations and therefore not applicable to the sudden termination of an established commercial relationship and applying French law insofar as "Article L. 442-6, I, 5° of the Commercial Code is a rule of economic public order and is recognized in that respect as a mandatory rule of public law within the meaning of private international law"; CA Grenoble, 5 September 2013: declaring inapplicable the law of Luxembourg as stipulated in the contract insofar as deliveries took place on the territory of France and that the contract has sufficient connection to France, with Article L. 442-6 applicable to the parties as a mandatory provision of public law.

<sup>158</sup> Cass. 1re civ., 26 September 2012, No 11-26.022.

<sup>159</sup> Cass. 1re civ., 25 March 2015, No 13-27.264.

<sup>160</sup> Cass. 1re civ., 7 October 2015, LawLex151216; also see, in exclusive distribution, Cass. com., 11 May 2017, LawLex17880, stressing that a jurisdiction clause in an international exclusive distribution contract is not contrary to Article [25 of Regulation No 1215/2012] merely on the ground that it is imposed on only one of the parties.&#10;

<sup>161</sup> Case C-352/13 Cartel Damage Claims, Judgment of 21 May 2015, LawLex15644.



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domiciled in a Member State may be sued in another Member State in the courts for the place of performance of the obligation in question (Art. 7(1)(a)). The place of performance of the obligation in question is, for the sale of goods, the place in a Member State where, under the contract, the goods were delivered or should have been delivered and in the case of the provision of services, the place in a Member State where, under the contract, the services were provided or should have been provided (Art. 7(1)(b)). The French courts applying the provisions under former Regulation No 44/2001 considered that an exclusive distribution contract was not the same as a contract for the sale of goods or a contract for the provision of a service and that the court having jurisdiction should be designated in application of [Article 7(1)(a)]<sup>162</sup>. The obligation in question referred to in Article 7(1)(a) had to be determined, by virtue of the conflict rule laid down in Article 4 of the Rome Convention of 19 June 1980 on the law applicable to contractual obligations, replaced by current Article 4 of Regulation No 593/2008 of 17 June 2008 (Rome I), by the law of the country of the party required to effect the characteristic performance. But, according to the Court of Cassation, this performance was that of the supplier who undertook to guarantee the exclusive distribution of his products to the reseller. The Court of Justice did not uphold this analysis ruling that an exclusive distribution agreement constitutes a contract for the supply of services, of which the characteristic performance is that which is provided "by the distributor which, by distributing the supplier's products, is involved in increasing their distribution". Such contracts are thus governed by the rules of jurisdiction under Article [7(1)(b)]<sup>163</sup>. The Court of Cassation subsequently aligned itself with that position. Specifically referring to the Court of Justice ruling relative to a "distribution agreement concluded further to a selection process and containing specific stipulations concerning distribution on the French territory" of a supplier's products, it laid down the principle that the rule of jurisdiction pursuant to Article 5(1)(b) of Brussels I (now replaced by Article 7 of Regulation No 1215/2012) must apply, excluding Article 5(1)(a) of the same regulation<sup>164</sup>.

The issue is even more complicated where a claim is brought for sudden termination of an established commercial relationship on the basis of Article L. 442-6, I, 5° of the Commercial Code and the parties disagree about whether the matter relates to contract (within the meaning of Article 5(1)(b) of Regulation No 44/2001, now Article 7(1)(b) of Regulation No 1215/2012) or tort (with regard to Article 5(3) of said regulation, now Article 7(2)). Although such actions are generally qualified as tort

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<sup>162</sup> Cass. 1re civ., 27 January 2007, 5 March 2008 LawLex07184, LawLex08316; 16 April 2008, LawLex08529; 9 July 2008, LawLex081139.

<sup>163</sup> Case C-9/12 Corman-Collins SA, Judgment of 19 December 2013, LawLex131876; Case C-64/17 Saey Home & Garden NV/SA, Judgment of 8 March 2018, LawLex18386.

<sup>164</sup> Cass. 1re civ., 19 November 2014, LawLex141289; also see CA Paris, 14 December 2016, LawLex1715.



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actions in the internal legal order<sup>165</sup>, this qualification does not apply pursuant to the regulation, with the concepts of tort or contract being interpreted autonomously in that context. **The Court of Justice, in a request for a preliminary ruling from the Paris Court of Appeal<sup>166</sup> has ruled that an action for damages founded on a sudden termination of an established commercial relationship is not a matter relating to tort, delict or quasi-delict if a tacit contractual relationship existed between the parties, demonstrated by factors such as the existence of a long-standing business relationship, the good faith between the parties, the regularity of the transactions and their development over time expressed in terms of quantity and value, any agreements as to prices charged and/or discounts granted, and the correspondence exchanged<sup>167</sup>.**

### 2) Applicable law<sup>168</sup>

More often than not, the parties will have jointly agreed to the law applicable to their exclusive distribution contract although sometimes they have not, in particular in the context of de facto relations or incomplete contracts, in which case determining the applicable law may give rise to endless disputes. One difficulty derives from the need to determine whether the dispute is of a contractual nature and subject in that case to the Rome I Regulation of 17 June 2008 or is a matter relating to tort and thus comes under the Rome II Regulation of 11 July 2007. The issue is particularly sensitive given that most of the litigation relating to terminations brought before the French courts is based on the termination of an established commercial relationship which is definitely regarded as a matter relating to tort in internal law, but which has not been clarified by the Court of Justice in light of the European rules.

But as the classification of matters relating to contract and tort are, in EU law, independent of national classifications<sup>169</sup>, the European judicature may not uphold them<sup>170</sup>.

Article 3 of the Rome I Regulation enshrines the principle of the parties' freedom of choice of the law applicable to the contract. This choice may be express and take the form of an *electio juris* clause, or tacit, and arise from the terms of the contract or from the circumstances of the case.

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<sup>165</sup> Cass. com., 18 January 2011, LawLex1183; Cass. com., 20 May 2014, LawLex14700.

<sup>166</sup> CA Paris, 7 April 2015, LawLex15000484.

<sup>167</sup> Case C-196/15 Granarolo SpA, Judgment of 14 July 2016, LawLex161361.

<sup>168</sup> CHRISTOU, *International Agency, Distribution and Licensing Agreements*, Sweet & Maxwell, 2011.

<sup>169</sup> Case C-189/87 Kalfelis v Schröder and others [1988] ECR p. 5565; Case C-26/91 Handte, Judgment of 17 June 1992; Case 26/76 Eurocontrol [1976] ECR p. 1541, LawLex092082; Case 29/76 LTU v Eurocontrol [1976] ECR p. 1541; Rome II Regulation, recital 11.

<sup>170</sup> The Paris Court of Appeal recently referred a question for preliminary ruling to the Court of Justice on relating to territorial jurisdiction: CA Paris, 7 April 2015, LawLex15484.



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Where the parties have not chosen the applicable law, the Rome I Regulation clearly determines which law shall govern the contract (Article 4(1)): a contract for the sale of goods is governed by the law of the country where the seller has his habitual residence; a contract for the provision of services is governed by the law of the country where the service provider has his habitual residence; for a franchise contract, the law of the country where the franchisee has his habitual residence; for distribution agreements, the law of the country where the distributor has his habitual residence. Other types of contracts are governed by the law of the country where the party required to effect the characteristic performance of the contract has his habitual residence (Article 4(2)). The choice under the regulation in favor of the law of the country of the distributor conflicts with the case law of the Court of Cassation, which makes distribution contracts subject to the law of the supplier<sup>171</sup>.

Obligation arising out of dealings prior to the conclusion of a contract are governed by the Rome II Regulation<sup>172</sup>, of which the principle is laid down in Article 12(1), entitled "Culpa in contrahendo" of either jurisdiction the law that applies to the contract or that would have been applicable to it had it been entered into. Where the applicable law cannot be determined on that basis, Article 12(2) provides that it can be either: a) the law of the country in which the damage occurs, irrespective of the country in which the event giving rise to the damage occurred and irrespective of the country or countries in which the indirect consequences of that event occurred; b) the law of the country where the parties have their habitual residence in the same country at the time when the event giving rise to the damage occurs; c) where it is clear from all the circumstances of the case that the non-contractual obligation arising out of dealings prior to the conclusion of a contract is manifestly more closely connected with a country other than that indicated in points (a) and (b), the law of that other country.

Finally, if the dispute concerns an issue of tort liability, it falls within the scope of the Rome II Regulation.

### 3) Overriding mandatory provisions (lois de police)

The existence of mandatory provisions, the immediate application of which is necessary to safeguard interests regarded as crucial by a country or the international community may prevent the application of the law chosen by the parties. Adopting the definition of Francescakis, the Rome I Regulation defines overriding mandatory provisions as "provisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organization, to such an

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<sup>171</sup> Cass. 1re civ., 23 January 2007, LawLex07184.

<sup>172</sup> Regulation No 864/2007 of 11 July 2007 on the law applicable to non-contractual obligations.



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extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the contract under this Regulation" (Article 9). Although overriding mandatory provisions of the law of the forum cannot be restricted (Article 9(2)), foreign mandatory provisions are subject to special rules: effect may be given to the overriding mandatory provisions of the law "of the country where the obligations arising out of the contract have to be or have been performed", insofar as "those overriding mandatory provisions render the performance of the contract unlawful" (Article 9(3)). The first civil chamber of the Court of Cassation adopts a position contrary to EU law by rejecting the application of the overriding provision of the law of the forum in the presence of jurisdiction clauses in favor of a foreign court<sup>173</sup>.

In French law, only those public policy provisions in the general interest (*ordre public de direction*) or those regulating the organization of the market - such as the rules of competition - make it possible to deviate from the intention of the parties. Those provision which fall in the category of public protection [*ordre public de protection*), which relate to private interests alone, are regarded as overriding mandatory provisions only in internal law.

Is Article L. 442-6 of the Commercial Code part of the public policy provisions in the general interest or for private interests? Legal doctrine appears to be divided and the cases law fluctuates<sup>174</sup>. The Court of Cassation and the Constitutional Council only not recognize the prerogatives of the Minister of the Economy on the basis of the protection of competition and of the market while the Paris Court of Appeal upholds the compatibility of Article L. 442-6 with the principle of the precedence of European competition law through its role of protecting competitors.

## CHAPTER 4

### SELECTIVE DISTRIBUTION

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<sup>173</sup> Cass. 1re civ., 6 March 2007, LawLex07349 and 22 October 2008, LawLex081850 regarding to the sudden termination of commercial relations of an exclusive concession agreement containing a clause conferring jurisdiction on the US courts.

<sup>174</sup> For an analysis, see CEPC (Commission for the Examination of Commercial Practices) Opinion No 15-08 of 17 April 2015 for an application for an opinion by a company on the position of the General Terms and Conditions of Sale and of the General Terms of Purchase. See also CA Paris, 8 October 2015, LawLex151245, finding in favor of the applicability of Article L. 442-6, I, 5° of the Commercial Code, law of the place where the harmful event occurred, for the sudden termination of a commercial relationship between a French distributor and a Dutch supplier, whereas the contract provided that it was subject to the law of the supplier.



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### Section 1 Lawfulness of network

#### I. System of control

##### B. Exemption

#### 4.17. Block exemption.

Regulation No 330/2010 of 20 April 2010<sup>175</sup>, which defines selective distribution in Article 1(e) lays down a presumption of lawfulness of the agreements in question when the supplier and the distributor respectively have a market share not exceeding 30% (Article 3), on condition that the agreement does not contain black or red clauses<sup>176</sup>. **Nevertheless, even when an agreement contains a hardcore restriction, it is not necessarily null and void. Like the Court of Justice previously in a matter relating to motor vehicle distribution<sup>177</sup>, the Court of Cassation considers that a non block-exempted agreement is not necessarily contrary to Article 101(1) TFEU<sup>178</sup>. It would, to infringe that provision, have to have a restrictive object or effect and affect trade between Member States.**

Purely qualitative selective distribution is generally considered as not subject to Article 101(1) TFEU, as it does not produce any harmful effects on competition as long as three conditions are met: mode of distribution justified by product quality, selection of distributors based on objective criteria, and respect for proportionality. On the other hand, quantitative selection, which adds other selection criteria that more directly limit the number of authorized resellers, especially by requiring minimum or maximum sales, or limiting the number of authorized distributors<sup>179</sup>, does come under the prohibition unless it qualifies for exemption.

#### II. Selection criteria

##### A. Qualitative criteria

##### 1° Content

##### b) Quality of distribution

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<sup>175</sup> EU Regulation No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices, OJEU L 102 of 23 April 2010, 1-7.

<sup>176</sup> Competition Council decision No 02-D-36 of 14 June 2002, LawLex022181; Cass. com., 20 March 2012, LawLex12497, ruling out an exemption where the prohibition of mail order sales is likely to restrict passive or active sales to end users. See also CA Paris, 19 September 2014, LawLex14945, according to which a former distributor may not rely on the discriminatory nature of a supplier's refusal to admit him to the network where the supplier, having a market share of below 30%, qualifies for exemption under BER 330/2010.

<sup>177</sup> CJEU Case 10/86 VAG France SA, Judgment of 18 December 1986, LawLex054435.

<sup>178</sup> Cass. com., 16 May 2018, LawLex18733 and LawLex18734.

<sup>179</sup> On the lawful nature of quantitative selection, Case 99/79 Lancôme v Etos [1980] ECR 2511, LawLex054076; 86/82 Hasselblad v Commission [1984] ECR 883, LawLex055391; 243/83 Binon v AMP [1985] ECR 2015, LawLex054001.



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### 4.30. Online sales/marketplaces.

According to the Competition Authority, the ban in principle on internet sales within a distribution network is unlawful<sup>180</sup>. The network developer cannot reserve, without discrimination, the marketing of its products to distributors having a brick and mortar outlet and refuse to authorize a distributor who is only present online while its standard contract includes no provision relating to mail-order sale or sale on the internet. The Competition Authority seems to adopt a position of principle favoring the prohibition of total and unlimited restrictions to online sales<sup>181</sup>, which it describes as hardcore restrictions since they limit both active and passive sales<sup>182</sup>, or as restrictions by object<sup>183</sup>. **It adopts a broad interpretation of indirect restrictions on online selling. Thus, the obligation for resellers to provide "hand delivery" for only the most dangerous products in a range of outdoor power equipment was considered to be a *de facto* prohibition of online selling constituting a restriction by object<sup>184</sup>.** However, it accepts the granting of individual exemptions in theory provided that the manufacturer shows a sufficient contribution to economic progress<sup>185</sup> which however would appear almost impossible to demonstrate in view of the requirements laid down in the recent case law<sup>186</sup>.

However, a supplier may impose restrictions on internet sales where such restrictions are proportionate to the objective sought and comparable to those applied in the distributors' brick and mortar outlets<sup>187</sup>. A supplier may thus require quality standards for the use of the website to resell its goods, just as it would require such standards for its stores or for catalogue selling or for advertising and promotion in general<sup>188</sup>. **According to the Paris Court of Appeal, the network may make the sale of luxury goods on the internet subject to the requirement of having at least one physical store without any restriction of**

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<sup>180</sup> Competition Council decision No 06-D-28 of 5 October 2006, LawLex061998. See also Case C-439/09 Pierre Fabre Dermo-Cosmétique, LawLex111588.

<sup>181</sup> Competition Council decision No 07-D-07 of 8 March 2007, LawLex07334.

<sup>182</sup> Competition Council decision No 08-D-25 of 29 October 2008, LawLex081872. The enforcement of the Council's decision has been stayed insofar as the order to modify its selective distribution contracts in order to authorize the online sales of its products by authorized distributors is likely to generate significant costs borne by the supplier and its distributors, and to substantially modify the consistence and nature of the network, such as it currently is, making a return to the previous situation difficult even unlikely in case of quashing of the decision: CA Paris, 18 February 2009, LawLex09460.

<sup>183</sup> Competition Authority decision No 12-D-23 of 12 December 2012, LawLex122443.

<sup>184</sup> Competition Authority decision No 18-D-23 of 24 October 2018, LawLex181583.

<sup>185</sup> Competition Council decision No 07-D-07 of 8 March 2007, LawLex07334, pt 94; No 08-D-25 of 29 October 2008, LawLex081872, pt 83.

<sup>186</sup> Case C-439/09 Pierre Fabre Dermo-Cosmétique, LawLex111588; CA Paris, 31 January 2013, LawLex13119; Competition Authority decision No 18-D-23 of 24 October 2018, LawLex181583.

<sup>187</sup> Competition Council decision No 06-D-28 of 5 October 2006, LawLex061998: the Authority approved the prohibition on applying loss-leader pricing or any promotional offers likely to challenge the high quality of the products. Compare No 07-D-07 of 8 March 2007, LawLex07334: selective distribution contracts of cosmetics raise competitive concerns where they provide for restrictions to the internet sale such as the obligation to create a website dedicated only to the sale of those products, to promptly answer to consumers' questions, to limit the number of products sold to each purchaser, or where they organize a control of advertising or references on search engines which is excessive compared to the legitimate objective of protection of the brand image.

<sup>188</sup> Guidelines on Vertical Restraints, para. 54.



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competition, since at the present time, consumers still express the need to be advised, to test the products and to take immediate possession of them in an environment consistent with their brand image, which cannot be provided by a general website where cut price luxury goods and everyday items are sold side by side<sup>189</sup>. Nevertheless, a supplier who is unable to demonstrate to the court the criteria applicable to internet sales cannot bring a liability action against a network member having sold products online without prior authorization<sup>190</sup>.

Generally, internet selling forces suppliers to review their commercial policy in order to guarantee the brand image of their products while adapting to the conditions of virtual sales. Issues concerning dedicated areas, shop-windows, surface, qualified staff, full product assortment, specific cash desk or brand environment are in effect treated differently. On the internet, the manufacturer may make the possibility of links to other websites depend on its prior approval whether those sites are commercial or non-commercial, impose a graphic charter which enables visual presentation of the products in line with the image of its products<sup>191</sup> and control the content of the website and the product environment<sup>192</sup>. To guarantee a delivery time which is satisfactory for consumers, the supplier may require internet resellers to have sufficient stocks<sup>193</sup>. Although the network leader may reserve internet sales to members of the network<sup>194</sup>, it cannot reserve those sales to itself alone by reason of the obligation of mutual fairness and the need for a reasonable sharing of the results of efforts made by all the network members<sup>195</sup>. Even if there is no damaging presentation or usurpation of the status of authorized distributor, the fact that a third party to the network sells products on the internet covered by a selective distribution network constitutes unfair competition<sup>196</sup> where the reseller does not justify the lawfulness of its purchases but submits vague invoices or invoices that do not relate to the products in question<sup>197</sup>. The mere fact of breaching the imperviousness of the distribution network is an act of parasitism<sup>198</sup>. Furthermore, the use

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<sup>189</sup> CA Paris, 28 February 2018, LawLex18367.

<sup>190</sup> CA Lyon, 7 May 2015, LawLex15628

<sup>191</sup> T. com. Nanterre, 4 October 2000, LawLex023266.

<sup>192</sup> T. com. Paris, 26 July 2007, LawLex071887; T. com. Paris, 31 October 2007, LawLex071916; TGI Paris, 13 February 2008, LawLex081935; T. com. Paris, 30 June 2008, LawLex081061: "The setting-up of selective distribution networks makes it possible to control the setting and framework of the sale of the goods concerned, the display setting on eBay is very variable, and brands therefore lose the control of the sale setting of their goods"; CA Paris, 11 July 2008, LawLex081918.

<sup>193</sup> Competition Council decision No 06-D-24 du 24 July 2006, LawLex061617.

<sup>194</sup> Competition Council decision No 07-D-07 of 8 March 2007, LawLex07334; CA Paris, 18 April 2008, LawLex08573; T. com. Paris, 3 June 2008, LawLex09737.

<sup>195</sup> For a joint interest representation contract: T. com. Bobigny, 29 January 2008, LawLex08173.

<sup>196</sup> CA Paris, 3 October 2014, LawLex141166.

<sup>197</sup> TGI Strasbourg, 8 January 2008, LawLex08222 and LawLex08223; CA Paris, 18 April 2008, LawLex08573: "[...] where a purchase is not lawful, reselling the products in dispute on an internet website knowing the existence of the selective distribution network, characterizes unfair competition [...]".

<sup>198</sup> T. com. Paris, 30 June 2008, LawLex081061.



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of the internet, a mere means of communication which cannot in itself constitute a relevant market or a sales outlet, does not make it possible to bypass the ban on resale outside the network<sup>199</sup>. The liability of certain internet platforms having undermined the selective networks in the luxury sector has thus been incurred by reason of their status as online brokers<sup>200</sup>. The prior existence of a brick and mortar outlet or the launching of a new product<sup>201</sup>, although constituting total restrictions to online sale, may, according to French courts, be used to exclude pure players from distribution<sup>202</sup>. The conditions of development of online distribution would longer appear to be a mere transposition of the conditions applied to brick and mortar outlets, and are sometimes specific to internet sales alone<sup>203</sup>. Even though such clauses have been upheld in numerous cases where their validity was contested, they would create a serious legal risk for undertakings adopting them given the rigor the courts have demonstrated in ruling against bans on internet sales.

The decision-making practice of the French competition authorities initially prohibiting all clauses banning the sale of the contract goods on online marketplaces<sup>204</sup> seemed excessive and sometimes contrary to the very principles of selective distribution. The most recent developments in favor of the freedom for members of a selective distribution network to sell on marketplaces seem to be particularly questionable.

The premise of a selective distribution system is that i) network members have an obligation to respect the image of the contract goods and the conditions of their distribution by complying with the

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<sup>199</sup> T. com. Nanterre, 4 October 2000, LawLex023266: a trader who is willing to sell on the internet perfumery products sold through a selective distribution network must previously request authorization from the manufacturer; Cass. com., 14 March 2006, LawLex06857: "[...] the creation of an internet site is not similar to the establishment of a sales outlet in the protected sector [...]."

<sup>200</sup> T. com. Paris, 30 June 2008, LawLex081061: "[...] eBay, in its capacity as broker, does not enjoy a derogatory status in respect of its liability and therefore falls within the general civil liability system like any trader", See by contrast, Vivastreet platform which was not recognized the status as host, therefore exempting it from any liability for frauds committed through its site.

<sup>201</sup> CA Paris, 18 April 2008, LawLex08573: "Pacific Création does not impose any general ban on the sale of its goods on the internet and does not exclude this selling method; [...] it is therefore possible for it, within its selective distribution network, to reserve to its distributors who have had a brick and mortar outlet for more than one year the distribution of its goods through the internet, and that condition should not be classified as a hardcore restriction; [...] likewise, the fact for Pacific Création to test only in brick and mortar outlets the launching of its new products cannot be indicted insofar as that restriction is limited in time to a maximum of one year".

<sup>202</sup> CA Paris, 16 October 2007, LawLex071575: "[...] "the Festina Or brand, [...] has grounds to require, in order to maintain a high quality image, in particular through an efficient after-sale service, and to guarantee the setting-off of its goods, that internet selling take place only as a complement of a brick and mortar outlet in the very interest of consumers"; CA Paris, 18 April 2008, LawLex08573: "[...] Pacific Création does not impose any general ban on the sale of its goods on the internet and does not exclude this selling method; [...] it is therefore possible for it, within its selective distribution network, to reserve to its distributors who have had a brick and mortar outlet for more than one year the distribution of its goods through the internet, and that condition should not be classified as a hardcore restriction; [...] likewise, the fact for Pacific Création to test only in brick and mortar outlets the launching of its new products cannot be indicted insofar as that restriction is limited in time to a maximum of one year".

<sup>203</sup> CA Paris, 18 April 2008, LawLex08573.

<sup>204</sup> Decision ordering provisional measures, Competition Authority No 14-D-07 of 23 July 2014, LawLex142294 and No 15-D-11 of 24 June 2015, LawLex15887, relative to the Samsung network, referring to the substantive examination of the clause prohibiting sales on marketplaces due to its potentially anticompetitive character; Press Release of 18 November 2015, noting the removal by Adidas of the clause in its contracts banning sales on marketplaces; CA Paris, 2 February 2016, LawLex16258, interim application, holding that the ban on sales on marketplaces or other online platforms may, unless there is objective justification, constitute a hardcore restriction.



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contractual obligations and the selection criteria without being able to authorize third parties to distribute the contract goods, ii) that the economic balance of the network should be preserved and guaranteed by the quantitative limitation of the number of points of sale if the head of the network considers it appropriate and iii) it is permitted under competition law i.e. the market share of the supplier and the distributor is less than 30%. The freedom to sell on internet marketplaces that the courts appear to be establishing is totally contrary to those three principles.

Many marketplaces do not provide the conditions in terms of presentation and valorization of products compatible with the rules of selective distribution<sup>205</sup>. The position of the competition authorities has lacked coherence in this respect: they accepted the networks' freedom to self-organize and the imperatives relating to the creation of a brand image but at the same time required manufacturers to mix their products, without any particular enhancement, with those of other brands not chosen by them and which did not necessarily belong to the same range of goods, on websites where they had no power to define the aesthetics or the rules of presentation and which often practiced aggressive pricing policies, or discount prices, whereas the recent case law also recognizes the right to refuse to accept the discount websites.

Similarly, it has always been accepted in competition law that a distributor under a selective distribution agreement should perform the contractual obligations itself and may not appoint sub-distributors or sub-agents without the agreement of the supplier<sup>206</sup>, or enter into agreements with undertakings operating in the territory agreed for the distribution contracts and sales and after sales services for the contract goods without the consent of the supplier<sup>207</sup>. Without those rules, the selective distribution network could no longer be controlled.

Marketplaces are presented as merely the agents of network distributors. In the light of the general rules of selective distribution, network members cannot however add points of sale without the agreement of their supplier. In addition market places are probably not mere agents. In reality, they generally identify as genuinely autonomous undertakings who decide themselves which distributors they will reference and the extent of the range of products they intend to offer for sale. Rather than being a transparent extension

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<sup>205</sup> Acceptance of a refusal to approve a website due to its ads relative to its practice of applying discounts: CA Paris, 25 March 2014, LawLex141777; 13 January 2016, LawLex1670.

<sup>206</sup> Explanatory Brochure for Motor Vehicle Regulation No 1415/95, question 11; Explanatory Brochure for Motor Vehicle Regulation No 1400/2002, authorizing three-tier distribution networks with the consent of the supplier.

<sup>207</sup> Motor Vehicle Regulation No 1415/95, Article 31.



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of the network members, marketplaces are actual, independent trading companies which define their own commercial policies.

Finally, the freedom to sell on marketplaces flies in the face of the recognized right for suppliers below the exemption thresholds for exemption to define quantitatively as they see fit the number of their points of sale required to reach their customers. To accept the unlimited freedom to sell on a marketplace is to deny the supplier the right to quantitatively build its network which is an essential component of quantitative selective distribution.

Doubtlessly influenced by the conclusions of the Commission in its final report on the e-commerce sector of May 2017, the French authorities backed down and ruled that the sales on non-approved platforms constituted a manifestly unlawful disturbance<sup>208</sup>, in the context of a network established as lawful by the Competition Authority in a commitments decision<sup>209</sup>. The subsequent recognition by the Court of Justice of the legality of the ban by a supplier on authorized distributors using, in a discernible manner, third-party platforms or market places for internet sales of its luxury products, should consolidate this change of direction<sup>210</sup>. According to the Court of Justice, such a prohibition is legitimate in order to guarantee that the goods will be exclusively associated with the authorized distributors in the minds of consumers and is an appropriate means for the supplier to check that the goods will be sold online in an environment that corresponds to the qualitative conditions that it has agreed with its authorized distributors in the absence of a contractual relationship between the supplier and third-party platforms enabling the supplier from being able to require, from the third-party platforms, compliance with the quality conditions that it has imposed. Lastly, the prohibition does not exceed what is necessary to achieve the objective of preserving a luxury image when the supplier does not ban the internet sale of the contract products outright, but only the use of third-party platforms that operate in a discernible manner towards consumers. In a later application on a similar question, the Paris Court of Appeal aligned itself to the position of the EU court<sup>211</sup>. Going further than the Court of Justice although in line with the interpretation of the Commission<sup>212</sup>, the Paris Court of Appeal has even held that the marketing of cosmetics can be prohibited on third-party platforms, whether or not they are regarded as

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<sup>208</sup> Cass. com., 13 September 2017, LawLex171426, quashing CA Paris, 2 February 2016, LawLex16258, cited above.

<sup>209</sup> Competition Council decision No 07-D-07 of 8 March 2007, LawLex07334.

<sup>210</sup> CJEU, Case C-230/16 Coty Germany GmbH Judgment of 6 December 2017, LawLex18317.

<sup>211</sup> CA Paris, 28 February 2018, LawLex18367.

<sup>212</sup> Competition Policy Brief 1/2018 - "EU competition rules and marketplace bans: Where do we stand after the Coty judgment?", 4 April 2018.



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luxury goods<sup>213</sup>. The Competition Authority has fallen in line with this trend, holding that the prohibition of sales on online marketplaces could also be justified for the sale of outdoor power machinery because of the technical specificities and dangerousness of such products<sup>214</sup>.

### Section 3 Relations between the parties

#### **II. Termination of contract**

##### A. Ordinary termination

#### **4.64. Notice period.**

Pursuant to the principle of contractual freedom, each party may put an end to an indefinite-term contract at any time without having to justify the grounds for such termination where a reasonable notice period is observed<sup>215</sup>. Thus, the network creator may unilaterally decide to terminate an indefinite-term contract without grounds where this contract provides for such a right in favor of each of the contracting parties in consideration of the observance of a notice period<sup>216</sup>. A manufacturer reorganizing its network is also entitled to terminate its selective distribution contracts as long as it has complied with a notice period in line with the norms in the trade<sup>217</sup>, but that notice period must comply with the reasonable notice period requirements pursuant to Article L. 442-6, I, 5° of the Commercial Code.

The reasonable notice period must take into account the length of the relationship, the volume of business, and also the activity sector concerned<sup>218</sup> and the fact that the products carry the distributor's own brand<sup>219</sup>. The supplier is in breach of his obligations where a notice of two and a half months is given for a relationship having lasted more than ten years where the distributor was led to believe that a new contract would be forthcoming<sup>220</sup>. **Where notice has been given it must be performed in conditions**

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<sup>213</sup> CA Paris, 13 July 2018, LawLex181096, ruling on referral from Cass. com., 13 September 2017, LawLex171426.

<sup>214</sup> Competition Authority decision No 18-D-23 of 24 October 2018, LawLex181583.

<sup>215</sup> CA Paris, 21 January 1993, LawLex025969; 1 March 2017, LawLex17416 and LawLex17417.

<sup>216</sup> See CA Paris, 6 March 2003, LawLex032265, which considers that a 6-month notice is reasonable.

<sup>217</sup> T. com. Cannes, 5 September 1996, LawLex024728; T. com. Paris, 2 April 1999, LawLex020148 (law on commercial negotiation): a four-month notice period is insufficient where the production cycle spreads on a six-month period; T. com. Paris, 25 September 2008, LawLex081934: A supplier cannot terminate a relationship having lasted more than ten years by only giving the distributor a notice period of two months and a half although it maintained the distributor in the illusion of the signature of a new contract.

<sup>218</sup> CA Amiens, 30 November 2001, LawLex020025 (in the case of a distributor's own brand, the notice period to be complied with is twice the normal notice period); CA Paris, 11 April 2002, LawLex020002: an established commercial relationship relating to advertising operations prepared several months in advance cannot be terminated without notice period given in due time; Cass. com., 12 March 2002, LawLex020039: the fact for an undertaking to give a notice period for termination of fifteen days to a contracting party with whom it has been bound for more than twenty years is an obviously unlawful disturbance.

<sup>219</sup> CA Paris, 23 March 2011, LawLex11780: luxury goods sector.

<sup>220</sup> T. com. Paris, 25 September 2008, LawLex081934.



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which, if not identical, are at least similar to those enjoyed prior to the termination. Nevertheless, an authorized distributor is precluded from claiming that the manufacturer has failed to comply with the notice obligation by refusing to deliver orders placed where the contract stipulates that the manufacturing deadlines for the products in question, which are not standardized, can be very long and that the supply cycles in the notice period are not found to be less frequent than those observed during the performance of the contract<sup>221</sup>. This is the case where a distributor has sold non-authentic products or refused to ensure the after-sales service in breach of its contractual obligations<sup>222</sup>. However, the termination is sudden when it purports to sanction an incident which, at the time of its occurrence, gave rise only to a call to order for the future and the contract was subsequently renewed<sup>223</sup>.

Where there are joint and several debtors, the letter of termination must be sent to each of them on an individual basis<sup>224</sup>.

### 4.66. Effects.

At the end of the contract, the former distributor must return any contract goods and advertising material that has remained in its possession. If it does not give back the whole stock in its possession at the term, it commits a breach of contract<sup>225</sup>. Likewise, a former member of the selective distribution network cannot, pursuant to the contract, keep on reproducing the logo of the brand on its website, continue to refer to itself as an authorized distributor or offer the sale of new products bearing that brand without being guilty of unfair competition<sup>226</sup>. It has however been held that former members of the repairer network of an auto manufacturer who unsuccessfully tried to have removed from the internet references to themselves as authorized repairers, are not liable for advertisements continuing to associate their names with that of their former supplier's brand<sup>227</sup>.

The former reseller who alleges that it meets the new selection criteria cannot require the resumption of a former contract relationship and must apply for a new authorization<sup>228</sup>. Initially the courts considered that where the termination of the contractual relationship resulted from the distributor's wrongful behavior, the supplier was not be required to accept its application and could justify that refusal to

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<sup>221</sup> T. com. Paris, 29 June 2016, LawLex18605.

<sup>222</sup> CA Angers, 31 January 2006, LawLex062467.

<sup>223</sup> CA Paris, 10 April 2013, LawLex13696.

<sup>224</sup> CA Paris, 30 June 2000, LawLex025314.

<sup>225</sup> CA Aix-en-Provence, 6 May 2003, LawLex034024.

<sup>226</sup> T. com. Saint-Brieuc, 12 October 2009, LawLex093212.

<sup>227</sup> Case C-179/15 Daimler AG v EGYÜD Garage, Judgment of 3 March 2016, LawLex16467.

<sup>228</sup> CA Paris, 31 January 2002, LawLex024498.



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authorize by the applicant's earlier wrongful behavior<sup>229</sup>. The imposition of a period of a ten years before a new application could be submitted was held lawful<sup>230</sup>. Now the courts consider that the principle of prohibition of perpetual contracts and the right to terminate a commercial relationship of indefinite duration preclude a terminated distributor from immediately obtaining approval after applying on the sole grounds that it meets the selection criteria<sup>231</sup>.

Some suppliers have included with the termination of a distributor publicity measures aimed at informing the public and encouraging other network members to comply with their obligations. A representative of the supply thus may inform the customers of terminated distributors of the end to their relations and give them the detail of other authorized distributors to ensure the maintenance and follow-up of the contract goods<sup>232</sup>. Excessive publication, given its costs and volume, is nevertheless a misconduct which incurs the civil liability of its author<sup>233</sup>. A court-ordered publication pronounced as a sanction cannot become the pretext for a campaign of denigration by the supplier<sup>234</sup>.

# CHAPTER 5

## MOTOR VEHICLE DISTRIBUTION

### Section 4 Termination of contract

#### I. Extraordinary termination

##### A. Causes

#### 5.54. Absence or transfer of showroom.

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<sup>229</sup> The refusal to authorize a former distributor terminated for misconduct is lawful: CA Paris, 25 February 2004, LawLex062084; Cass. com. 19 September 2006, LawLex061929. See, also, in the motor vehicle sector: Cass. com., 15 September 2009, LawLex093094: a manufacturer may refuse to authorize a candidate even if it complies with all the qualitative criteria required to integrate the network, where it is a former dealer terminated for serious misconduct.

<sup>230</sup> CA Versailles, 29 February 1996, LawLex031550.

<sup>231</sup> See especially T. com. Paris, 29 June 2016, LawLex18605; 21 February 2018, LawLex18320.

<sup>232</sup> CA Paris, 15 September 2010, LawLex101043.

<sup>233</sup> T. com. Aix-en-Provence, 1 December 1991.

<sup>234</sup> CA Aix-en-Provence, 13 March 1997, LawLex021286.



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Under Regulation No 1475/95 of 28 June 1995, the lack of specific premises for the sale of the manufacturer's motor vehicles was a legitimate cause for termination of the contract<sup>235</sup>. The use by the dealer of a single showroom for the sale of competing brands, whereas it had undertaken under contract to reserve it to the dealer's brand<sup>236</sup> or the mere transfer of the premises against the supplier's advice<sup>237</sup> thus allowed the manufacturer to put an immediate end to the contract. Absolute multi-branding established by Regulation No 1400/2002 of 31 July 2002 prevented the manufacturer from requiring the dealer to display the brand's motor vehicles in a separate area. At most, the manufacturer could display the motor vehicles "in brand-specific areas of the showroom in order to avoid brand confusion"<sup>238</sup>. Breach of that obligation was a legitimate cause for termination.

Since 1 June 2013, the sale of new motor vehicles has come under the regulation on vertical restraints. Distribution agreements can once again include non-compete obligations prohibiting distributors from reselling competing brands in general. Authorized distributors may therefore be prevented from trading from different premises or from opening a new store in another place. **Thus, the modification by the distributor of its place of establishment without prior authorization from the manufacturer, which in addition is now in a temporary space not meeting the standards of the brand, justifies the immediate termination of the contract<sup>239</sup>.**

## II. Ordinary termination

### A. Notice period

#### 5.60. Contractual or reasonable notice period.

Where the agreement has an indefinite term, block exemption was subject to the ordinary termination period of at least two years for both parties (Regulation No 1400/2002, Article 3(5)(b))<sup>240</sup>. Since 1 June 2013, ordinary termination has no longer been subject to a fixed notice period to benefit from the block exemption. The obligation to comply with a reasonable notice period will nevertheless still be the rule. In effect, each party may terminate an indefinite-term contract at any time provided that it complies

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<sup>235</sup> Cass. com., 16 April 1996, LawLex025563, dismissing the appeal lodged against CA Paris, 7 April 1994, LawLex025389.

<sup>236</sup> CA Paris, 14 November 2002, LawLex03737.

<sup>237</sup> CA Paris, 14 November 1994, LawLex025421.

<sup>238</sup> Regulation No 1400/2002 of 31 July 2002, OJEC L 203 of 1 August 2002, Article 1(1)(b) and recital 27.CA

<sup>239</sup> CA Paris, 7 February 2018, LawLex18254.

<sup>240</sup> Where the agreement did not fall within the scope of European competition law, the parties could set a notice period of less than two years, see CA Aix-en-Provence, 26 October 2001, LawLex03568; CA Paris, 2 September 2010, LawLex10988.



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with a reasonable notice period and does not commit an abuse of right<sup>241</sup>. Furthermore, the use of the two-year notice remains commonplace; on the one hand, a number of contracts concluded under Regulation No 1400-2002 are still in force, and on the other, the codes of practice of the ACEA<sup>242</sup> and JAMA<sup>243</sup> associations recommend a notice period of two years.

Compliance with the contractual notice period is in principle sufficient to validate the termination of the contract<sup>244</sup>, unless the duration of the contractual notice period is less than the legal notice required by Article L. 442-6 of the Commercial Code, which is not usually the case for motor vehicle distribution contracts due to the two-year notice period stipulated in Regulation No 1400/2002, which remains the norm even after its expiry. Until the entry into force of Regulation No 1400/2002, it was accepted that compliance with the notice period exempted the manufacturer from any obligation to justify the termination<sup>245</sup> or at least made it irrelevant whether or not the reasons given were accurate<sup>246</sup>. Compliance with the notice period also exempted the manufacturer from any liability by reason of investments incurred by the dealer shortly before the notification of the termination<sup>247</sup>, provided that they were spontaneous investments by the dealer which could be re-used as part of another exploitation<sup>248</sup>, and not investments required by the manufacturer and specific to the brand. If it had complied with the contractual notice period, the manufacturer could neither be blamed for having not kept its dealers informed of its reorganization projects<sup>249</sup> nor of having compromised the terminated dealer's chances of reconversion by placing it in an inferior negotiating position with a purchaser of its business, insofar as the purpose of the notice period is precisely to allow it to begin its reconversion<sup>250</sup>. By contrast, the termination of a distribution contract by reason of the termination of the contract between the manufacturer and the importer does not constitute a force majeure event that justifies shortening the contractual notice period where the importer has obtained the continuation of the

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<sup>241</sup> CA Versailles, 14 December 1995, LawLex025516: the termination without notice period of an indefinite-term distribution contract is abusive by reason of its sudden character; Cass. com., 20 January 1998, LawLex025089; 7 October 1997, LawLex025053.

<sup>242</sup> European Automobile Manufacturers Association.

<sup>243</sup> Japanese Automobile Manufacturers Association.

<sup>244</sup> T. com. Paris, 28 September 1989, LawLex025758; CA Paris, 22 October 1999, LawLex025244.

<sup>245</sup> CA Paris, 11 December 1990, LawLex025815; TGI Paris, 27 November 2002, LawLex03640.

<sup>246</sup> CA Paris, 26 January 2005, LawLex053766.

<sup>247</sup> CA Paris, 19 May 1993, LawLex026004; 4 July 1996, LawLex025590.

<sup>248</sup> CA Versailles, 15 May 1998, LawLex025128 approved by Cass. com., 6 June 2001, LawLex024370; 2 July 1998, LawLex025137, approved by Cass. com., 22 May 2001, LawLex024906; CA Paris, 4 June 2003, LawLex032288; 19 June 2003, LawLex04778.

<sup>249</sup> T. com. Paris, 25 October 1999, LawLex025245; CA Paris, 4 June 2003, LawLex032288; 15 September 2004, LawLex042112. Contra, See T. com. Paris, 29 November 1999, LawLex025255.

<sup>250</sup> Cass. com., 6 May 2002, LawLex024624. See also CA Paris, 4 June 2003, LawLex032288.



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supplies under specific conditions<sup>251</sup>. These solutions remain applicable post 1 June 2013 as the vertical restraints regulation does not provide for any obligation of a contractual nature.

What will happen when a distributor terminates the contract without complying with the contract notice period? According to the trial courts, the distributor who fails to comply with the notice period is not liable where the notice was given solely in the distributor's interest and the supplier was able to find a new distributor rapidly<sup>252</sup>. **More reasonably, other courts have accepted the existence of harm for the supplier, to which however they award compensation not according to the loss of gross margin but to the expected profit on sales where the measure occurs in the context of a recession<sup>253</sup>. In other circumstances, the harm is compensated on the basis of the manufacturer's loss of margin on variable costs until the appointment of a new distributor or the normal term of the relationship<sup>254</sup>.**

The systematic non-application of the obligation of compliance with the notice period, which is disadvantageous for the supplier and favors the distributor, seems abnormal. It goes against the principle of the binding force of contracts which applies to both parties and seeks to minimize the disruption of the supplier's sales due to the distributor's failure to comply with the notice period when leaving the network.

### D. Obligation to state reasons

#### **5.66. No obligation to state reasons.**

Under Regulation No 1400/2002 of 31 July 2002, for suppliers to qualify for block exemption they were required to give notice of termination in writing and to include objective and transparent reasons for the termination decision (Article 3(4))<sup>255</sup>. Even if it imposed a requirement going further than general contract law<sup>256</sup>, the regulation did not require reasons for termination for breach of contract or any review by the courts of the appropriateness of the manufacturer's decision<sup>257</sup>, but merely an explanation of the decision, which could be due to circumstances which were legitimate and which could even be

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<sup>251</sup> CA Paris, 5 February 2003, LawLex032863.

<sup>252</sup> CA Chambéry, 8 April 2014, LawLex141871.

<sup>253</sup> CA Grenoble, 22 February 2018, LawLex18358.

<sup>254</sup> CA Paris, 12 September 2018, LawLex181295.

<sup>255</sup> T. com. Limoges, 25 June 2003, LawLex032860 approved by CA Limoges, 10 March 2004, LawLex04949; T. com. Nanterre, 1 June 2004, LawLex041651, which indicates that the obligation to state reasons only relates to terminations held after 1 October 2003.

<sup>256</sup> See T. com. Paris, 2 December 2013, LawLex131770, which restates that in contract law a supplier may proceed with an ordinary termination by complying with the contractual notice period without having to give reasons for that decision even if it was necessary to terminate the agreement in order to be in conformity with Regulation No 1400/2002.

<sup>257</sup> T. com. Pontoise, 25 September 2007, LawLex071516: the control by the court on the reasons for the termination must be limited to checking their pro- or anticompetitive character, and cannot relate to the appropriateness of the decision.



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unrelated to the co-contracting party per se. According to the trial courts, the purpose of the obligation to state reasons was only to ensure that terminations were not carried out to restrict competition. Apart from such considerations, the courts were not required to verify the accuracy of the reasons provided by manufacturers<sup>258</sup>. The need to reorganize the distribution network to comply with the Vertical Restraints Regulation has nevertheless been considered a valid reason to terminate the contract in light of the requirement to give reasons<sup>259</sup>. **Similarly, the termination of a motor vehicle distribution contract due to the implementation of a new policy of growth based on the development of the range and new requirements to strengthen customer satisfaction, notified to the whole of the network in France and in Europe, was not considered to be determined by anticompetitive motives<sup>260</sup>.**

Since 1 June 2013, the distribution of new motor vehicles has come within the scope of application of the Vertical Restraints Regulation. Court decisions rendered before Regulation No 1400/2002, which made the lawfulness of the termination conditional upon the manufacturer complying with a contractual or reasonable notice period<sup>261</sup> now once again apply insofar as contracts no longer have to contain an obligation to provide reasons for termination<sup>262</sup>. Like previously, stating reasons, even fallacious ones, will therefore no longer incur the supplier's liability<sup>263</sup> **since the court is not required to review the legitimacy of the grounds for termination given by the manufacturer<sup>264</sup>**. Likewise, the fact that a dealer's conduct has been exemplary i.e. always meeting commercial targets and realizing all investments required to promote the brand image, will not challenge the validity of the termination<sup>265</sup>. In contrast,

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<sup>258</sup> T. com. Paris, 13 February 2014, LawLex14297. The court thus considers that the supplier had fulfilled its obligation in respect of the requirement of the regulation by complaining to the dealer about its poor commercial performances, its inadequate bank guarantee and the selling of vehicles to final customers before having paid the supplier for them, CA Paris, 4 February 2015, LawLex15146; see also T. com. Paris of 16 June 2015, LawLex15772; CA Paris, 24 June 2015, LawLex15837.

<sup>259</sup> CA Paris, 11 May 2016, LawLex16965.

<sup>260</sup> Cass. com., 29 March 2017, LawLex17627.

<sup>261</sup> T. com. Paris, 28 September 1989, LawLex025758 approved by CA Paris, 11 December 1990, LawLex025815; 3 March 1995, LawLex024268; Cass. com., 6 June 2001, LawLex024370; 6 May 2002, LawLex024621; T. com. Bobigny, 24 January 2003, LawLex031195; T. com. Versailles, 14 November 2003, LawLex034429; 9 June 2006, LawLex061373; CA Versailles, 31 January 2006, LawLex07273; CA Paris, 10 January 2018, LawLex1864.&#10;

<sup>262</sup> CA Paris, 19 October 2011, LawLex111723: a manufacturer giving notice of termination in an ordinary termination is not required to give reasons for that decision; CA Paris, 15 January 2014, LawLex1433, ruling that in the automobile sector, a termination due to the reorganization of the network does not have to be justified as long as does not reflect the implementation of an anticompetitive practice. T. com. Paris, 24 February 2016, LawLex16416, holding that the absence of reasons for the termination of an open-ended contract is not unlawful where the supplier has granted the dealer the two-year contractual notice period.

<sup>263</sup> TGI Paris, 2 February 1995, LawLex025444; CA Versailles, 22 May 1998, LawLex024911; Cass. com., 20 February 2007, LawLex07227; 6 November 2007, LawLex071778. Contra, see prior court decisions controlling the stated reasons: CA Paris, 5 November 1990, LawLex025806 (no cleaning of premises); Cass. com., 5 April 1994, LawLex025387 (dealer's intention to withdraw); 20 January 1998, LawLex025089 (insufficient sales); CA Versailles, 25 November 1999, LawLex025254 (dealer's deficiency); CA Paris, 11 May 2016, LawLex16965.

<sup>264</sup> Cass. com., 29 March 2017, LawLex17627.

<sup>265</sup> CA Paris, 22 March 2002, LawLex024699.



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a grievance which was not mentioned in the termination letter may not subsequently be invoked to justify the measure<sup>266</sup>.

### IV. Sudden termination of established commercial relationship

#### 5.73. Application of Article L. 442-6, I, 5° of the Commercial Code to motor vehicle distribution.

Until 1 June 2013, in order to qualify for block exemption by virtue of the successive motor vehicle regulations, automobile distribution agreements had to provide for a minimum notice period for both ordinary contract terminations and for the non-renewal of fixed-term contracts. In principle, compliance with the contractual notice period should have been sufficient for the termination for the contract to be lawful<sup>267</sup>. However, relying on Article L. 442-6, I, 5° of the Commercial Code, the courts have assumed the authority to assess the reasonable nature of contractual notice periods<sup>268</sup>. Extending the scope of application of Article L. 442-6, I, 5° in this way raises the question as to its relationship to EU law.

It is difficult to reconcile the fact that a notice period provided for under European competition law can be called into question by a national rule which also pursues the aim of protecting the market. Thus, it has been held that a dealer whose contract has been terminated for network reorganization with one year's notice could not rely on Article L. 442-6, I, 5° of the Commercial Code to challenge the duration of the notice period as the provision must be interpreted in light of European law which takes precedence over national law<sup>269</sup>. This should also be the case with regard to the two-year notice period under Regulation No 1400/2002. The Versailles Court of Appeal chose not to adopt that position, considering that the notice periods set out in Regulation No 1400/2002, which is not intended to replace the domestic public policy provisions of Article L. 442-6, I, 5° of the Commercial Code, could not serve as a reference for the assessment of the minimum notice period owed to the victim of a sudden termination of an established commercial relationship<sup>270</sup>. Likewise, the Court of Appeal in Limoges held that Article L. 442-6, I, 5°, which provides for the possibility to grant a longer notice period than the motor vehicle regulation, is not contrary to the provisions of the latter as it only provides, in its preamble, for minimum periods<sup>271</sup>. The Paris Court of Appeal concurred with that opinion, finding that since Article 101 and

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<sup>266</sup> CA Paris, 18 May 2016, LawLex16955.

<sup>267</sup> T. com. Paris, 28 September 1989, LawLex025758.

<sup>268</sup> See especially CA Versailles, 4 September 2012, LawLex122118.

<sup>269</sup> CA Paris, 11 May 2011, LawLex11935, LawLex11936, LawLex11937, LawLex11946, LawLex11947.

<sup>270</sup> CA Versailles, 4 September 2012, cited above.

<sup>271</sup> CA Limoges, 9 February 2012, LawLex12294. The court maintained its position in the judgment rendered following referral from the Court of Cassation (14 May 2013, LawLex13830), CA Limoges, 18 February 2015, LawLex15227.



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102 TFEU pursue objectives which are different from those pursued by Article L. 442-6, there is nothing to prevent the court from assessing the reasonable character of the two-year notice period granted by a car manufacturer under Regulation No 1400/2002 with regard to the length of previous relations<sup>272</sup>. Those decisions defy all logic since the only legal issue that needs to be posed is whether a contract which is fully exempted under EU law can be prohibited by a rule of national law. In principle, as both texts are aimed at protecting the market, the answer must be no, it cannot. **This position, although contestable insofar as the courts are challenging the principle of precedence of European law, was nevertheless upheld by the Court of Cassation<sup>273</sup>.**

Apart from those cases, the courts consider that the notice period given to the distributor must, to comply with Article L. 442-6, I, 5°, be of sufficient duration for the dealer to develop new business. Thus, a period of two years is regarded as reasonable even for a commercial relationship of over thirty years in light of the concrete possibilities to transform the business open to the terminated dealer<sup>274</sup>. Likewise, a six-month period for the termination of an automobile distribution agreement of indefinite duration was held to be reasonable within the meaning of Article L. 442-6, I, 5° although it was less than the period provided for in the motor vehicle regulation, as the terminated multi-brand dealer had already found an alternative solution prior to the expiry of the contractual notice period and was able to increase revenues during that period<sup>275</sup>. A distributor also cannot complain of having received no notice of termination at all where such termination was notified in two letters sent by the manufacturer more than a year before which clearly stated that the contract would not be renewed once it arrived at its term, even if it did not rule out the possibility of re-examining the dealer's application for a new contract<sup>276</sup>. **Article L. 442-6, I, 5° allows for a sudden termination on the grounds of non-performance of obligations by the other party. The termination of the established commercial relationship is not "sudden" where it occurs in the context of the dealer's extended failure to meet its financial obligations<sup>277</sup>. However, a failure to comply with the standards of the brand that has been tolerated by the manufacturer for several years may not be invoked to justify a sudden termination of the established commercial relationship<sup>278</sup>. To be effective, the notice period granted must be respected; relations must be maintained if not under**

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<sup>272</sup> CA Paris, 15 January 2014, LawLex1433; 2 July 2014, LawLex14777 and 24 June 2015, LawLex15837; 11 May 2016, LawLex16965.

<sup>273</sup> Cass. com., 5 July 2016, LawLex161293, upholding on this issue CA Limoges, 18 February 2015, LawLex15227.

<sup>274</sup> CA Paris, 25 January 2012, LawLex12183. But see CA Limoges, 18 February 2015, LawLex15227, granting a notice period of 36 months for a 44-year relationship.

<sup>275</sup> CA Paris, 2 September 2010, LawLex10988.

<sup>276</sup> Cass. com., 14 May 2013, LawLex13830; and on referral: CA Limoges, 18 February 2015, LawLex15227.

<sup>277</sup> T. com. Ajaccio, 2 October 2017, LawLex171875.

<sup>278</sup> CA Paris, 25 October 2017, LawLex171717.



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the exact same, then at least under similar conditions during that period. According to case law, a manufacturer does not comply with the notice period when it makes the signing of a new contract subject to the dealer achieving higher sales in that period than those stipulated in the objectives clause of the contract<sup>279</sup>.

The Court of Cassation's recent case law based on Article L. 442-6, I, 5° of the Commercial Code has tended to make contractual relations increasingly rigid. The courts now assess the duration of the required notice period and subsequently the compensation owed in the event of insufficient notice automatically from the date of receipt of the termination letter by the distributor<sup>280</sup> without taking into account the successful transformation of the distributor's business prior to the date on which the contract should have theoretically terminated, which in practice can lead to the awarding of compensation where no loss has been suffered, an outcome which is difficult to justify with regard to a provision intended to repair harm. After handing down several judgments in which it expressed its disagreement, considering that the realities of a reorganization or the absence of harm to the terminated partner were factors that should be taken into account when assessing the amount of notice required<sup>281</sup>, the Paris Court of Appeal now appears to wish to go back to the position adopted by the Court of Cassation<sup>282</sup>.

## V. Termination of agency contract

### 5.74. No triangular relationship.

In France, as in most larger countries with a low or average population density, motor vehicle distribution networks are generally organized into a primary network of dealerships and a secondary network of motor vehicle agents.

The motor vehicle agent has no direct legal connection with the manufacturer<sup>283</sup>. The affixing of its signature on the agency contract followed by the mention "for approval" is a mere technical approval that certifies that the agent meets the conditions required to represent its brand<sup>284</sup>. The manufacturer

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<sup>279</sup> Cass. com., 29 March 2017, LawLex17627.

<sup>280</sup> Cass. com., 9 July 2013, LawLex131090.

<sup>281</sup> CA Paris, 28 January 2016, LawLex162250, LawLex16227; 29 January 2016, LawLex16284.

<sup>282</sup> CA Paris, 15 November 2017, LawLex171871, holding that the compensation awarded to the dealer cannot be reduced merely by reason of the fact that it found a new brand to represent in the course of the notice period when no return on investment is expected before the end of that period and LawLex171889: the fact that the dealer has found another brand to commercialize in the course of the notice period does not reduce the compensation owed insofar as the manufacturer is unable to demonstrate that this representation offset the dealer's loss of revenue in respect of sales of products of its brand; 15 March 2018, LawLex18515.

<sup>283</sup> T. com. Bordeaux, 8 August 1995, LawLex2300205487.

<sup>284</sup> T. com. Bordeaux, 8 August 1995, LawLex2300205487; CA Rennes, 10 March 2009, LawLex09994.



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cannot therefore be held liable for the termination, such liability being attributable to the dealer<sup>285</sup> or the agent if the latter instigated the termination<sup>286</sup>. The manufacturer's liability can only be sought where it is established that it is at the origin of the contractual relationship from which the agent's loss arose<sup>287</sup> or that the dealer has set up an inter-dependency between the contracts and ensured that the agency contract follows the main contract<sup>288</sup>. Thus, the termination of a dealer agreement can lead to the termination of the independent repairer's agency agreement by reason of their inter-dependency, where the breaches having justified the termination of the dealer agreement undermine the loyalty, confidence and partnership on which the relationship is based<sup>289</sup>.

Traditionally case law has held that where the contractual notice period is complied with, the termination of the agency contract is not abusive<sup>290</sup>. Now the courts will find that the contractual notice period must however be in relation to the length of the commercial relationship between the parties. It has also been held that there was no sudden termination of the established commercial relationship where a dealer terminated a contract which had been pursued for fifteen years, in giving its agent, who was not in a situation of dependence with respect to the dealer, a six-month contractual notice period<sup>291</sup>. In practice, dealers often give agents the two year' notice as provided by the former motor vehicle regulations. Similarly, a two-year notice period is considered sufficient with regard to an established commercial relationship of sixteen years' duration<sup>292</sup>. In addition, where the two-year notice period is respected, the court does not have to assess the merits of the grounds relied upon by the dealer<sup>293</sup>. However, a dealer whose contract is terminated with two years' notice in the expectation of the proposal of a new contract in compliance with the new motor vehicle regulation and who has, for that reason, terminated the contract binding it to its agent, is guilty of a sudden termination of an established business relationship where it only informs the agent at the end of the notice period given that no new contract will be signed with the latter<sup>294</sup>. However, the fact that a service agent was the only member of

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<sup>285</sup> CA Toulouse, 22 June 2004, LawLex041670; CA Bordeaux, 22 April 2003, LawLex04499; T. com. Nanterre, 30 March 2005, LawLex055536; T. com. Lille, 15 April 2009, LawLex091731.

<sup>286</sup> CA Toulouse, 22 June 2004, LawLex041670.

<sup>287</sup> CA Paris, 19 September 2013, LawLex131358.

<sup>288</sup> CA Versailles, 16 October 2007, LawLex071583.

<sup>289</sup> CA Pau, 3 October 2013, LawLex131455.

<sup>290</sup> CA Paris, 15 October 1999, LawLex033231.

<sup>291</sup> CA Rennes, 16 January 2007, LawLex071110.

<sup>292</sup> CA Paris, 19 September 2013, LawLex131358.

<sup>293</sup> CA Versailles, 11 September 2018, LawLex181264.

<sup>294</sup> CA Paris, 27 February 2017, LawLex17422.



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the network not to have been offered a new contract is not sufficient to establish the existence of discrimination incurring the contractual liability of the dealer<sup>295</sup>.

Most motor vehicle agent contracts include a stipulation which withdraws the status of commercial agent for the activity of representative for the sale of new vehicles carried out as a secondary activity to that of independent trader for the sale of spare parts and auto repairs. **In addition, a vehicle service agent may demand the notice period provided for by Article L. 442-6, I, 5° of the Commercial Code and not the period provided for in Article L. 134-11 for commercial agents, insofar as the contract describes him as an independent trader who acts in his own name and for his own account, and he acts only in an ancillary capacity as an agent for the sale of vehicles<sup>296</sup>.**

## VI. Termination of authorized repairer contract

### 5.75. Termination for fault.

In accordance with Article 1224 (formerly 1184) of the Civil Code, breaches by authorized repairers in the execution of the contract may justify its termination by the manufacturer. This is the case where the authorized repairer is listed in the yellow pages and on the internet as a dealer for the sale of new vehicles<sup>297</sup>, carries out such sales, even without any advertisement<sup>298</sup>, or contacts a third party to the network claiming to be an authorized distributor, and proposing training courses for the reparation of branded vehicles and the supply of diagnosis tools reserved for members of the network, and has allowed that party to win a call for tenders to the detriment of network members<sup>299</sup>. The termination of repairer's agency contract is also justified in the case of a refusal to submit to the required skills assessment for continued authorization<sup>300</sup>. When the repairer is also authorized to sell new vehicles under a second contract, the termination of a dealer agreement also terminates the authorized repairer contract if it is stipulated that a breach of one of them will extend to the other in the case of a fault undermining fair trading, the trust and the partnership between the parties<sup>301</sup>. **On the other hand, a manufacturer causes a manifestly unlawful disturbance ("trouble manifestement illicite") that the court can remedy by ordering the continued performance of the contract, when it terminates the relationship on the basis of**

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<sup>295</sup> CA Paris, 27 June 2018, LawLex181024.

<sup>296</sup> CA Paris, 13 October 2016, LawLex161692.

<sup>297</sup> CA Paris, 22 January 2013, LawLex1387; T. com. Paris, 13 February 2014, LawLex14297; CA Paris, 18 January 2017, LawLex17114.

<sup>298</sup> T. com. Paris, 21 June 2017, LawLex171411.

<sup>299</sup> CA Versailles, 20 October 2015, LawLex151321, specifying that the contract may be terminated without notice, even if this is contractually required when it is not materially possible for the repairer to remedy the breach in question.

<sup>300</sup> T. com. Bordeaux, 8 November 2013, LawLex131633.

<sup>301</sup> Cass. com., 10 February 2015, LawLex15371, upholding CA Pau, 3 October 2013, LawLex131455. Cf. in the absence of an interdependence clause between the contracts, CA Paris, 10 November 2016, LawLex161878.



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its interpretation of a clause relating to the obligations of the members of the network in terms of signage, which is particularly unfavorable to the repairer having regard to the location of his establishment in relation to the street, even though the stipulation invoked does not necessarily permit it<sup>302</sup>. Likewise, an auto manufacturer cannot terminate the contract of an authorized repairer for breaches by the latter during the performance of the previous contract and which are sanctioned by contractual penalties<sup>303</sup>.

As is the case in a number of areas, it is tempting to invoke Article L. 442-6, I, 5° of the Commercial Code to contest the termination. Nevertheless, the provision can only be relied on if the relationship at issue is an "established" one. This is obviously not the case for a contract of only five months' duration<sup>304</sup>. In addition, the discretion of the court means that, where the claim is brought on the basis of Article L. 442-6, I, 5° of the Commercial Code, it may not only increase but also reduce the duration of the contractual notice period in an authorized repairer contract where it does not take account of the brevity of the commercial relationship in question<sup>305</sup>. Lastly, insofar as only losses resulting from the sudden nature of the termination can be repaired on the basis of Article L. 442-6, I, 5° of the Commercial Code, the decline of a repairer's after-sales activity cannot be indemnified on that basis<sup>306</sup>.

## VII. Consequences of termination

### B. Compensation for loss

#### 2° Assessment of the loss

### 5.89. Dealer's loss.

The compensation for the distributor's loss in respect of a sudden termination of its contract must be limited only to the harm resulting from the sudden nature of the termination<sup>307</sup> (and should not extend to harm related to the termination itself) which is generally assessed as the amount of the margin that would have been made during the notice period. **The courts for a long time, and not without criticism, indemnified the loss of gross margin.** It has thus been held that only the gross operating surplus, which reflects the economic result achieved by the dealer, may be used as a basis for calculation of the loss

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<sup>302</sup> CA Paris, 10 November 2016, LawLex161878.

<sup>303</sup> CA Paris, 27 March 2017, LawLex17638.

<sup>304</sup> CA Paris, 22 January 2013, cited above.

<sup>305</sup> Cass. com., 22 October 2013, LawLex131543.

<sup>306</sup> Cass. com., 5 July 2016, LawLex161293.

<sup>307</sup> CA Paris, 20 January 2011, LawLex11120.



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resulting from an abusive termination<sup>308</sup>. However, where the dealer had announced its intention to transfer its business, its loss could only correspond to the loss of gross margin it could have achieved during the two years of notice period that it could have claimed<sup>309</sup>. Likewise, the dealer's loss cannot be calculated in view of the average gross margin it achieved in the last three years of operation where its results constantly decreased during that period<sup>310</sup>. Some courts even considered that the compensation should not concern the loss of margin over the two years of notice period but only the loss of the opportunity to pursue business relations in those two years, by taking account, if necessary, of the deterioration of the dealer's financial situation during that period<sup>311</sup>. **More reasonably, the Court of Appeal of Paris has returned to this position and advocated, in its "*fiches méthodologiques*" (Fact Sheets) on the compensation of economic loss<sup>312</sup>, that account be taken not of the loss of gross margin, but the loss of margin on variable costs, i.e. the turnover after deduction of costs which have not been borne as a result of the decline in activity. This principle is now applied in many cases<sup>313</sup>, even if certain chambers of the Court of Appeal continue to refer to gross margin.**

Moreover, the dealer's loss cannot be assessed in view of the value of its business where it could rapidly redeploy<sup>314</sup>. By contrast, where the termination of its contract was conducted in such a way that it was impossible for it to transfer its business or to find another brand to represent, the dealer must be compensated for the loss of its business<sup>315</sup>.

**Finally, under Article 2224 of the Civil Code, a compensation claim cannot be brought more than five years after the event giving rise to the harm or the knowledge of it by the dealer<sup>316</sup>. In this regard, the courts have stated that the fact that the manufacturer was willing to provide the distributor with assistance in connection with the closure of a site does not constitute an acknowledgment of liability for the operating losses that the latter has suffered capable of interrupting the statute of limitations<sup>317</sup>.**

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<sup>308</sup> TGI Paris, 19 September 2006, LawLex062073; but see CA Grenoble, 4 October 2007, LawLex071517: the loss of a dealer that has been abusively terminated must be assessed not from the gross margin but from the net profit, less expenses and charges linked to the activity.

<sup>309</sup> CA Paris, 24 January 2008, LawLex081248.

<sup>310</sup> CA Paris, 15 April 2010, LawLex10472.

<sup>311</sup> CA Paris, 27 May 2010, LawLex10631.

<sup>312</sup> Fiche méthodologique (Fact Sheet) No 6, "Which concept of margin ?"

<sup>313</sup> CA Paris, 15 November 2017, LawLex171871.

<sup>314</sup> Cass. com., 3 July 2001, LawLex024957, on this issue quashing CA Paris, 27 May 1998, LawLex024958.

<sup>315</sup> Cass. com., 17 July 2001, LawLex024948, approving CA Paris, 10 December 1998, LawLex024947.

<sup>316</sup> T. com. Versailles, 8 September 2017, LawLex171460 and 7 March 2018, LawLex18394.

<sup>317</sup> T. com. Paris, 28 May 2018, LawLex18879.



## CHAPTER 6

# FRANCHISING

### **6.08. Impact of general distribution law and rules specific to franchises.**

In spite of its commercial success, franchising is currently undergoing significant legal challenges. Like all the other types of distribution network, its efficiency is undermined by the general rules of competition and distribution law intended to regulate the difficult relationship between the large retail distribution sector and suppliers, the application of which is extensive and includes all distribution agreements.

The introduction of binding provisions of general scope designed to resolve the particular case of the mass food retail distribution sector has led to an unnecessary intransigence affecting the whole of the French economy and in particular franchise agreements.

The law governing the termination of established commercial relationships has led, in this area as well as others, to the extension of notice periods incompatible with economic efficiency and the need to adapt to the constraints of competitiveness since suppliers are not effectively protected against the de-listing of their products by large retail distributors<sup>318</sup>.

The rules covering significant imbalance, like for other types of distribution agreements, weaken franchise agreements by creating considerable legal uncertainty but they have not led to a better balance in the relations between retail groups and suppliers.

The single commercial agreement ("convention unique") and the principle of fixed rates for its duration (1 year) advocated in the government's interpretation of the Hamon Law forces suppliers into a situation where they have two types of contract in their relationship with franchisees: a usual fixed or open-ended contract and an artificial one-year contract in order to meet the requirements of the single commercial agreement. The reform of affiliation agreements establishes a new regime of post-contractual non-compete clauses which is stricter than European Union law in this area, which violates the principle of precedence.

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<sup>318</sup> The large retail chains regularly subject their suppliers to calls for tender which renders their relations precarious and prevents suppliers from benefitting from the protection afforded under Article L. 441-6, I, 5° of the Commercial Code.



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Under the ordinary distribution and competition law there are therefore a lot of unnecessary constraints for franchise networks.

The franchisee, who is assumed to be the weaker party in the contract, will be more easily able to get out of commitments made, notably by claiming that correct information was not supplied, that his consent was vitiated because of the abusive exploitation of his state of dependence vis-a-vis the franchisor, that the franchise agreement is in fact a standard form agreement ("contrat d'adhésion") creating an imbalance between the rights and obligations of the parties or that the franchisor has not provided any justification for the price of the contract goods or variations thereof.

The law with regard to franchises resulting from the application of the new law of contracts clearly does not make French law more attractive and will likely result in parties ensuring that international franchise agreements are made subject to foreign laws, with jurisdiction or arbitration conferred on foreign courts or arbitrators which are more respectful of the autonomy of the parties' intentions and the principle of the binding force of contracts.

In addition to that issue which applies to all distribution networks in fact we must add a further legal constraint specific to franchises. Even if there is no legislation specifically concerning franchises, with the pre-contract information requirement laid down by the Doubin Law not limited to franchise agreement but applicable to all contracts concluded in the common interest of both parties with the provision of distinctive signs and the stipulation of an obligation of exclusivity or quasi-exclusivity, the franchises are increasingly characterized by a specific set of legal rules that ultimately do not appear to be in their interest. Also, in the context of merger control, franchise networks are increasingly viewed as a single undertaking, which makes concentration operations between franchisees more and more difficult where there is a franchise brand with a strong presence in the same catchment area, even if the stores are operated by various independent traders.

The most worrying development in the law on franchises concerns labor law. In addition to the risk of reclassification, employment law tends to identify franchise networks as single entities, like integrated companies, although they are made up of independent traders. The reclassification obligation within the network is a strong indication of this trend. **This culminated in the introduction of employees' representative committees ("*instance de dialogue social*") in each franchise network<sup>319</sup>, treating franchisees'**

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<sup>319</sup> Article 64 of Law No 2016-1088 8 August 2016 known as the Law on Work (Loi Travail) or El Khomri Law (after Myriam El Khomri, Minister for Employment) resulting from amendment No 1721 introduced during debates in the General Assembly, on first reading of the law on new liberties and new protection for undertakings and employees and adopted Article 29 bis A of the draft law.



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stores as branches of the franchise when in fact they are independent businesses, the success of which depends on their managerial autonomy. The introduction of the reform was heavily criticized by legal commentators and by franchisors and franchisees. It reflects a strong trend in franchising law to treat the network as an integrated company contrary to the very foundations of the franchise. Luckily, those criticisms were taken on board: the employee representative committee was repealed by Law No 2018-217 of 29 March 2018<sup>320</sup>.

### Section 1 Lawfulness of network

#### **I. Restrictive practices**

##### **6.09. Resale price maintenance and abuse of dependence.**

Like other distribution contracts, franchise agreements are subject to competition law and in particular to rules relating to the prohibition of restrictive practices.

##### 1) Resale price maintenance

Article L. 442-5 of the Commercial Code prohibits per se any person imposing, directly or indirectly, a minimum on the resale price of a product or on the price of services or on a trading margin.

The mention of maximum resale prices is valid in the absence of practices purporting to impose them<sup>321</sup>. The franchisor may thus send a catalogue of recommended prices to its franchisees as long as they can adapt those prices to them<sup>322</sup>. Similarly, the franchisor is not guilty of RPM within the network when the rates communicated are maximum recommended prices and it offers the service to customize price lists for franchisees not wishing to adhere to those prices<sup>323</sup>. The provision of pre-established price lists and labels does not constitute resale price maintenance where franchisees have rooms for maneuver in fixing their resale price<sup>324</sup>. Occasional promotional campaigns are also not sufficient to characterize resale price maintenance<sup>325</sup>. Only the imposition by the franchisor of a minimum resale price is prohibited<sup>326</sup>. The absence of resale price maintenance in a franchise network is sufficiently established

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<sup>320</sup> Article 7 of Law No 2018-217 of 29 March 2018 ratifying various ordinances issued on the basis of enabling Law No 2017-1340 of 15 September 2017 to implement by ordinance the measures for the reinforcing of social dialogue, OJ, 31 March 2018.

<sup>321</sup> Cass. com., 10 January 1995, LawLex020316; CA Paris, 2 March 1999, LawLex023119.

<sup>322</sup> CA Paris, 28 January 1993, LawLex022622; CA Pau, 27 March 2002, LawLex024210.

<sup>323</sup> CA Paris, 29 June 2016, LawLex161211.

<sup>324</sup> CA Douai, 19 March 1998, LawLex020087.

<sup>325</sup> CA Paris, 3 September 2014, LawLex14857.

<sup>326</sup> Cass. com., 13 February 2001, LawLex020086.



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in view of the heterogeneous nature of margins achieved by its various members<sup>327</sup>. Likewise, the joint fixing between a franchisor and a franchisee of the price of a service has not been held unlawful where there is no evidence of any imposition of a minimum price or of the exertion of economic pressure<sup>328</sup>.

The franchisor incurs criminal liability if it exerts pressures on its franchisees to apply the recommended prices regardless of their form<sup>329</sup>, or inserts clauses in its contracts imposing the compliance with a floor price<sup>330</sup>. The contract may also be declared null and void<sup>331</sup>: any agreement deviating from Article L. 442-5, which is an economic public order provision, is null and void. Lastly, franchisees who are the victims of resale price maintenance practices by their supplier suffer from moral damage for which the supplier is bound to compensate<sup>332</sup>, even if they have taken part in committing the offense<sup>333</sup>.

### 2) Abuse of dependance

Like for other types of network, franchisees are no longer reluctant to rely on Article L. 442-6, I, 2° of the Commercial Code, which prohibits imbalanced terms in relations between professionals. According to case law, a clause is imbalanced where there is no reciprocity, disproportionate obligations are imposed or it is of a potestative nature. However, the reciprocity requirement is not absolute. Thus, the sole fact that a post-contractual non-compete clause imposed on a franchisee is not offset by an exclusivity arrangement in the course of the contract does not show an imbalance where the purpose of the clauses is different and although the former is inherent to franchises, the latter is not<sup>334</sup>. Similarly, the existence of an early termination for the sole benefit of the franchisor does not in itself constitute a significant imbalance within the meaning of Article L. 442-6, I, 2°, which is assessed in light of the overall balance of the contract<sup>335</sup>. Clauses that require the franchisee to make specific refurbishments to its point of sale do not characterize a significant imbalance in the rights and obligations of the parties when uniformity and common identity in the network constitute the consideration for the transmission of the franchisor's know-how and the latter can show that it has made similar investments for its branches<sup>336</sup>. The courts

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<sup>327</sup> CA Paris, 25 January 2006, LawLex08191.

<sup>328</sup> CA Nimes, 22 May 2003, LawLex0446.

<sup>329</sup> CA Amiens, 17 January 1995, LawLex020260; TGI Brest, 21 February 1995, LawLex020264.

<sup>330</sup> CA Paris, 13 November 1996, LawLex020029.

<sup>331</sup> See CA Pau, 22 June 1995, LawLex020284: an exclusive supply clause favors a resale price maintenance practice and results in the nullity of the franchise contract which includes it where it is used to deliver pre-labeled products, making it impossible for the franchisee to modify the price.

<sup>332</sup> CA Paris, 16 January 2002, LawLex03535.

<sup>333</sup> Cass. crim., 19 February 2003, LawLex03963.

<sup>334</sup> CA Paris, 14 December 2016, LawLex1717, upheld by Cass. com., 30 May 2018, LawLex18834.

<sup>335</sup> CA Paris, 3 May 2017, LawLex17855.

<sup>336</sup> CA Paris, 22 November 2017, LawLex171946.



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not only require the existence of an imbalance but also the subjection of one partner by the other to that imbalance. Such is not the case of a franchisee who can freely decide to enter into the contract proposed by the franchisor when at the date of the facts, the latter was the head of a network consisting of one single member<sup>337</sup>.

Other types of behavior sanctioned by Article L. 442-6 are sometimes invoked but actions rarely meet with success. A franchisor who makes the renewal of the contract subject to the acceptance by the franchisee of a 20% holding in its capital does not violate Article L. 442-6, I, 4° of the Commercial Code in the absence of evidence that it is a condition which is manifestly unreasonable concerning prices, payment deadlines, terms and conditions of sale or services not arising from the obligations of purchase and sale within the meaning of that provision<sup>338</sup>. The payment of a franchise fee has also been considered as not devoid of consideration within the meaning of Article L. 442-6, I, 1° of the Commercial Code insofar as this is usual in franchise agreements, and it pays for the concession of the franchise, the right to use the trade marks and for the know-how and initial training, which are the constituent elements of the concept proposed by the franchisor<sup>339</sup>.

## II. Restrictive agreements

### A. Prohibition

#### 4° Non-compete clause

### 6.17. Conditions of validity.

Franchise agreements often contain a non-compete clause restricting the freedom of the former franchisee by preventing it from exploiting a professional activity in competition with that of the franchisor for a limited period on a given territory. Non-compete clauses are inherent in franchising insofar as they guarantee the protection of know-how, which must only benefit network members, and give the franchisor the time to set up another franchisee in the exclusivity area. To avoid being caught by the ban on restrictive agreements, such clauses must remain proportionate to the objective they pursue, i.e. the protection of know-how, the identity and reputation of the network<sup>340</sup>. The Vertical Restraints Regulation makes the exemption of post-contract non-compete clauses subject to material, spatial and temporal limitations: the obligation cannot exceed one year as of the date of termination of

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<sup>337</sup> CA Paris, 17 May 2017, LawLex17895.

<sup>338</sup> CA Paris, 7 June 2017, LawLex171027.

<sup>339</sup> CA Paris, 17 May 2017, LawLex17895.

<sup>340</sup> Guidelines on Vertical Restraints, pt 190 (2): "A non-compete obligation on the goods or services purchased by the franchisee falls outside Article 101(1) when the obligation is necessary to maintain the common identity and reputation of the franchised network".



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the agreement, may only relate to goods or services in competition with the contract goods or services and must be limited to the premises and land from which the buyer has operated during the contract period. The non-compete obligation must also be indispensable to protect know-how transferred by the supplier to the buyer<sup>341</sup>. Thus, the prohibition on engaging in any similar trade for two years in the exclusivity area has been held excessive in relation to the objective of protection of know-how<sup>342</sup>. Likewise, a non-compete clause not essential to the protection of the franchisor's know-how - characterized by its low technicality level and the fact it is no longer technically accessible at the term of the contract - and which is not limited to the franchisee's premises, is not proportionate to the franchisor's legitimate interests and, as it is unable to benefit from an automatic exemption, is therefore void<sup>343</sup>.

The fate of disproportionate post-contractual non-compete clauses has been the subject of much debate. Should the court reduce the scope of application of such clauses thus making them fairer or simply void them with no reduction of their scope?

The analogy could be made in favor of the first option that in many areas of the law, the courts adopt a realistic and pragmatic approach simply by reducing the scope of provisions deemed disproportionate. This is usually the case for exclusive obligations of more than 10 years' duration in violation of the Law of 14 October 1941, now codified in Article L. 330-1 of the Commercial Code<sup>344</sup>, or for non-compete clauses in deeds of transfer<sup>345</sup>. In employment law too the Court of Cassation has moderated the scope of disproportionate non-compete clauses giving trial courts the power to limit the effect in the time, space or having regard to its other terms<sup>346</sup>. In matters relating to franchises, although the courts tend to have adopted different solutions<sup>347</sup>, the Court of Cassation has been stricter and would appear to have clearly opted for the second, more rigorous solution. If a non-compete clause is disproportionate, it is void, and it is not for the court to reduce its scope to a lawful level either of its own motion<sup>348</sup> or when requested to do so by the supplier<sup>349</sup>.

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<sup>341</sup> Article 5(3) of Regulation No 330/2010.

<sup>342</sup> CA Paris, 18 March 1997, LawLex022672: the technical level of the sale of clothes did not justify the inclusion of such a clause.

<sup>343</sup> CA Paris, 13 December 2017, LawLex172064.

<sup>344</sup> Cass. com., 10 February 1998, LawLex025103.

<sup>345</sup> CA Orléans, 30 January 2011, RG 13/01443.

<sup>346</sup> Cass. soc., 20 October 2008, No 07-42.035; 18 September 2002, No 00-42.904; 27 September 1989, No 86-43.701; Cass. com., 26 February 1970, No 69-40.191. Adde, Cass. soc., 26 February 1970 n° 69-40.191.

<sup>347</sup> In favor of a limitation of excessive clause: CA Paris, 26 juin 1997, LawLex025028: limitation from 2 years to 1; for a geographic limitation: CA Paris, 3 June 2011, LawLex111037. But see CA Aix-en-Provence, 18 October 2007, JCP E, 2008, 2172.

<sup>348</sup> Cass. com., 12 March 2002, LawLex020545.

<sup>349</sup> Cass. com., 30 March 2016, LawLex16710.



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### Section 3 Formation of contract

#### **6.31. General principles of contract law.**

To be valid, a franchise agreement must not only meet specific conditions such as the obligation of pre-contractual information where it contains exclusive or quasi-exclusive purchase obligations, but also the conditions of the general law on contracts. It has been held that the performance of a draft agreement by the franchisee even if though he had refused to sign it amounted to an acceptance of the franchise agreement<sup>350</sup>.

The absence of a condition of validity is penalized and the contract declared null and void. Nullity may also only be partial where the missing condition is not the decisive element of the franchise contract<sup>351</sup>. The nullity of the whole contract results in the repayment of expenses directly related to its performance<sup>352</sup> such as network entry fees, royalties, layout costs and specific investments which have not been recouped<sup>353</sup>. This does not however give the franchisee the right to compensation for the financial loss arising from the failure to obtain the commercial results it was entitled to expect through exploitation of the franchise<sup>354</sup>, **the loss of opportunity to make better use of its funds when the franchisee does not show that a better opportunity to contract with a third party was missed<sup>355</sup>, or its operating losses<sup>356</sup>**. Similarly, the nullity of the franchise agreement cannot result in the nullity of the loan agreement taken out to finance the business, unless the borrower brings evidence of the inseparable nature of those contracts<sup>357</sup>, or in the reimbursement of expenses incurred to develop the business or

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<sup>350</sup> Cass. com., 19 January 2016, LawLex16186.

<sup>351</sup> CA Nîmes, 22 May 2003, LawLex0446: the nullity of the resale price maintenance clause cannot result in the nullity of the whole contract where this clause only refers to one of the services provided by the franchisee and cannot be regarded as an impulsive and decisive cause of the franchise contract.

<sup>352</sup> CA Pau, 24 September 1998, LawLex024658: entry fees, fees of acquisition of the rights to lease and decorate the commercial premises and interest paid on borrowings taken out to fund these expenses; CA Paris, 26 October 2006, LawLex07759: entry fee, paid fees, layout costs and non-amortized specific investments.

<sup>353</sup> CA Paris, 30 June 2011, LawLex111373; 2 October 2013, LawLex131467; CA Paris, 10 September 2014, LawLex14936; CA Montpellier, 21 October 2014, LawLex141191; CA Paris, 16 November 2016, LawLex161971; but see Cass. com., 29 March 2017, LawLex17629, considering that the franchisor may, after the cancellation of the contract, retain a portion of the franchise fee when it also pays for the license agreement.

<sup>354</sup> Cass. com., 18 October 2011, LawLex111668; CA Montpellier, 21 October 2014, LawLex141191; CA Colmar, 14 March 2018, LawLex18532.

<sup>355</sup> Cass. com., 29 March 2017, LawLex17629.

<sup>356</sup> CA Paris, 16 November 2016, LawLex161971, cited above; CA Paris, 18 October 2017, LawLex171699; 17 January 2018, LawLex18142; Cass. com., 29 March 2017, LawLex17629; CA Colmar, 14 March 2018, LawLex18532.

<sup>357</sup> Cass. com., 13 April 2010, LawLex10475; 14 December 2010, LawLex101475; 15 February 2011, LawLex11304; cf. 12 July 2011, LawLex111255 but see CA Reims, 6 August 2013, LawLex131245. Cf. Cass. com., 12 July 2011, LawLex111255, finding that franchise and supply agreements of different durations concluded on the same day between the same parties are indivisible, where they provide for control by the franchisor over the franchisee's advertising implying that the products distributed by the franchisee are supplied by the franchisor or a



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compensation for payments not paid to a director of the franchisee undertaking<sup>358</sup>. **The franchisor is also not required to cover the investments borne by the franchisee when they enabled the latter to continue his activity after the termination of the initial contract<sup>359</sup>. Nullity does not exempt the franchisee from payment of goods ordered either<sup>360</sup>.**

A franchise agreement can also be cancelled, rather than terminated, with reimbursement of the entry fee where, as a result of its provisions, which are ambiguous and have been interpreted as against the franchisor who drafted the agreement, the obtaining of a lease by the applicant constitutes a condition subsequent<sup>361</sup>.

The reform of contract law as a result of the Ordinance of 10 February 2016 will have consequences on franchise agreements as it will on other types of distribution contracts. It will, inter alia, make it easier for franchisees to contest their contractual obligations by claiming to have had inadequate information at the time of the conclusion of the contract (Civil Code, new Article 1112-1), that the franchisor has abused their situation of dependence (Civil Code, new Article 1143), that they were required to agree to accept imbalanced obligations (Civil Code, new Article 1171) in the general terms of a franchise agreement similar to those in an adhesion contract (standard form contract) (Civil Code, new Article 1110), or that the franchisor has failed to show the legitimacy of the price or of price variations in the course of the contract (Civil Code, new Article 1164).

### I. Breakdown of negotiations

#### 6.32. Conditions of liability.

The franchisor may have its liability incurred for abusive termination of negotiations where, after having given its consent on the principle of a franchise contract and on the technical and financial conditions and the setting-up of it, it refuses to approve it without stating reasons some months before the opening<sup>362</sup>. Similarly, the termination of a franchise reservation agreement is imputable to the franchisor who, after accepting repeated postponements of the start of activity requested by the candidate, then fails to respond to the candidate's initial request for basic training<sup>363</sup>. **The franchisor who is unable to**

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corporation it controls; CA Paris, 18 Octobre 2017, LawLex171699, cited above, considering indivisible the franchise agreement and a contract for the rental of vehicles or the guarantee instrument, but not the deed of of transfer of the business.

<sup>358</sup> CA Colmar, 30 September 2015, LawLex151264.

<sup>359</sup> Cass. com., 29 March 2017, LawLex17629.

<sup>360</sup> Cass. com., 14 January 2014, LawLex1446.

<sup>361</sup> CA Paris, 25 September 2013, LawLex131415.

<sup>362</sup> T. com. Versailles, 22 June 2001, LawLex024945 approved by CA Versailles, 27 February 2003, LawLex033477.

<sup>363</sup> CA Douai, 2 July 2015, LawLex15909.



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establish that it carried out its mission of assistance in the finding of a point of sale and of approaching the local market is liable for the rescission of the pre-franchise memorandum and must refund the deposit paid by the candidate<sup>364</sup>. In turn, the applicant franchisee who, after having terminated discussions, carries on the exploitation of an establishment with the customer-base created during the pre-contract test phase, according to a similar concept, or makes use of the descriptive elements of the pre-contract information document provided by the franchisor to create an independent business and to free-ride on the latter's coat-tails by copying its ideas and concept<sup>365</sup>, commits an act of parasitism, even in the absence of direct competitive situation<sup>366</sup>. On the other hand, liability is not incurred where there has been no irrevocable commitment in sufficiently defined terms to conclude an agreement and there has only been an agreement in principle<sup>367</sup> or where the termination does not reflect the candidate's intention to take advantage of the reputation of a well-known chain when launching its business activity but is due to the fact that it became aware of the strict commercial terms imposed by the franchisor<sup>368</sup>. Moreover, a clause in a territory reservation agreement according to which the franchisor may retain the full amount of the sums paid by the candidate when he abandons the project is considered to be unfair due to the lack of reciprocity and the disproportionate nature of the sanction<sup>369</sup>.

## II. Pre-contract information

### A. Scope of application

#### 6.35. Renewal and transfer of contract.

According to the Court of Cassation<sup>370</sup>, Article L. 330-3 applies even in case of renewal of the franchise agreement, which may be tacit. The solution challenges the decisions of the trial courts which consider that the information had not to be re-provided where the signatories of the new contract are the same and the fundamental characteristics of the new contract are identical to those of the former<sup>371</sup>. According to case law, the mandatory nature of the provision of information required under Article L. 330-3 of the Commercial Code renders inoperative a waiver by the franchisee in the event of a renewal of contract<sup>372</sup>.

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<sup>364</sup> CA Paris, 16 March 2017, LawLex17571.

<sup>365</sup> CA Poitiers, 28 February 2017, LawLex17505.

<sup>366</sup> CA Nîmes, 17 April 2008, LawLex082193.

<sup>367</sup> Cass. com., 18 January 2011, LawLex1186.

<sup>368</sup> CA Douai, 29 June 2011, LawLex111379.

<sup>369</sup> CA Grenoble, 14 November 2017, LawLex171902.

<sup>370</sup> Cass. com., 9 October 2007, LawLex071569. See also CA Paris, 6 June 2018, LawLex18883.

<sup>371</sup> T. com. Paris, 13 January 1997, LawLex02000267; CA Paris, 20 September 1994, LawLex021544; 6 November 1998, LawLex025151. But see CA Paris, 23 November 2000, LawLex024680 which waives the pre-contract information obligation in case of acquisition of control of the franchisor where no new contract is entered into with the franchisees.

<sup>372</sup> CA Versailles, 18 September 2014, LawLex14960.



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Nevertheless, the court, in a more measured manner, considers that the non-delivery of a precontractual information document during the renewal of a franchise agreement does not vitiate the consent of the franchisee when the latter is well aware of the franchise, its network, its mode of operation and the local market<sup>373</sup>.

Where the franchise agreement is assigned, the franchisor is also required to again provide the pre-contract information<sup>374</sup>. **However, the placing into lease management of the franchisor's business does not give rise to an obligation to provide a new pre-contractual information document to the franchisee<sup>375</sup>.** The franchisee is itself subject to a pre-contract information duty in case of transfer of its contract to a third party, as far as the features and accounting books specific to the business it transfers are concerned<sup>376</sup>.

### C. Sanction

#### 1° Nullity

##### a) Requirement of vitiated consent

## 6.42. Principle.

The breach of Article L. 330-3 of the Commercial Code may render the franchise agreement null and void<sup>377</sup> despite the absence of specific provision for this. However, this is not an automatic nullity<sup>378</sup>: the nullity is incurred only if the franchisee's lack of information has vitiated its consent<sup>379</sup>.

In effect, according to Article L. 330-3 of the Commercial Code, information given by the franchisor is purported to enable the future franchisee to commit itself in full knowledge of the facts. If the information has been transmitted correctly<sup>380</sup> or if, despite the lack of delivery of the pre-contractual

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<sup>373</sup> CA Paris, 15 June 2016, LawLex161142.

<sup>374</sup> CA Rennes, 8 April 2014, LawLex141873

<sup>375</sup> CA Paris, 7 March 2018, LawLex18393.

<sup>376</sup> CA Metz, 23 September 2008, LawLex091752.

<sup>377</sup> Cass. com., 12 February 2008, LawLex08210: the sanction of the breach of the pre-contract information duty is annulment and not the termination of the contract, quashing on this issue CA Orléans, 26 October 2006, LawLex08171; CA Paris, 22 May 2008, LawLex082196; 18 June 1997, LawLex025680.

<sup>378</sup> See previous case law holding the automatic nullity: CA Paris, 24 March 1995, LawLex025457; 17 May 1995, LawLex03854; CA Montpellier, 4 December 1997, LawLex025075; 3 October 2000, LawLex025322.

<sup>379</sup> Cass. com., 2 December 1997, LawLex025073; 24 March 1998, LawLex025112; 19 October 1999, 3 decisions, LawLex024387, LawLex024388 and LawLex024389; 16 May 2000, LawLex024377; 22 October 2002, LawLex02000365; 20 March 2007, LawLex07360: a franchise contract cannot be annulled due to the sole fact that the franchisor has not given it the mandatory pre-contract information duty within the legal time-period.

<sup>380</sup> CA Colmar, 9 March 1990, LawLex025772; CA Douai, 21 March 1996, LawLex025555: Handing in of a serious setting-up survey; Cass. com., 20 October 1998, LawLex024399: optimistic but serious survey; CA Orléans, 1 March 1991, LawLex031666 approved by Cass. com., 14 January 2003, LawLex03654; CA Versailles, 13 May 2004, LawLex043491: complete documents and realistic forecasts, which the franchisee acknowledged being only indicative.



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information document, the candidate to the franchise had sufficient information to guarantee the integrity of its consent, there is no reason to annul the contract<sup>381</sup>. **Conversely, the court cannot dismiss a franchisee's action for a declaration of invalidity on the sole ground that the latter has acknowledged having received a complete pre-contractual information document, without itself ascertaining that such is in fact the case<sup>382</sup>.** As the validity of the consent given is assessed at the date of the conclusion of the contract, the franchisee may not rely on factors subsequent thereto to claim that his consent was vitiated<sup>383</sup>.

The voiding of the contract therefore requires the courts to assess the decisive character of the vice, whether fraud or mistake, the propensity for the candidate to be misled and the management qualities of the latter.

### 6.44. Fraud.

It is for the franchisee to bring evidence of the existence of fraudulent tactics<sup>384</sup>, the intentional nature thereof<sup>385</sup>, and vitiated consent<sup>386</sup> i.e. relating to the decisive element of the candidate's consent<sup>387</sup>. The documents provided by the franchisor must be properly drawn up using the relevant data about the local market<sup>388</sup>, without attempting to hide any losses suffered<sup>389</sup> or concealing its own lack of experience<sup>390</sup>.

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<sup>381</sup> See inter alia CA Paris, 11 December 1998, LawLex025161; 13 January 1999, LawLex025167; 24 September 2008, LawLex093634; Cass. com., 15 March 2011, LawLex11698; even if some missing information in the pre-contractual stage document has had the effect of distorting the estimates established by the franchisor, the court is required, before annulling the contract, to check if this failure has determined the consent of the candidate.

<sup>382</sup> Cass. com., 10 January 2018, LawLex1866; see also CA Nîmes, 14 June 2018, LawLex18943.

<sup>383</sup> CA Aix-en-Provence, 24 March 2016, LawLex16761; 12 May 2016, LawLex16996: the number of undertakings having left the network after the conclusion of the contract is not taken into consideration)

<sup>384</sup> Cass. com., 6 May 2002, LawLex024600; 14 June 2005, LawLex056646.

<sup>385</sup> CA Rennes, 22 March 2016, LawLex16692.

<sup>386</sup> CA Versailles, 20 October 2006, LawLex08187: evidence of the defect of the consent is on the franchisee, even if the non-performance of the information duty is established; CA Paris, 27 April 2000, LawLex025300. See also Cass. com., 14 June 2005, LawLex056646.

<sup>387</sup> CA Paris, 28 March 1991, LawLex025838; 26 March 1999, LawLex025197: a franchise contract must be annulled for deceit where the candidates have been misled by overly optimistic promises, without which they certainly would have not entered into any contract; 4 December 2003, LawLex042111: the supply of estimated accounts including serious mistakes, without which the franchisee would not have committed itself, results in the nullity of the contract; CA Paris, 9 May 2001, LawLex024812; CA Nîmes, 6 October 2005, LawLex051; CA Caen, 4 May 2005, LawLex06359: non-delivery of significant elements for the economic assessment of the transaction; CA Paris, 5 July 2006, LawLex062459: deficiencies of the information not related to an essential element the disclosure of which could have prevented the franchisee from committing itself; CA Aix-en-Provence, 27 March 2007, LawLex082191: the franchisor's conduct, who misleads the candidate by voluntarily concealing information likely to modify the decision to enter into the contract, given the failure of the former franchisee, is equipollent to deceit and justifies the cancellation of the franchise contract; CA Paris, 24 September 2008, LawLex093634; Cass. com., 3 April 2012, LawLex12542, ruling out the annulment of the contract where irregularities in the pre-contract information provided are not a decisive factor.

<sup>388</sup> CA Paris, 19 May 1999, LawLex025215.

<sup>389</sup> Cass. com., 14 December 1999, LawLex024385; CA Versailles, 6 March 1997, LawLex0200067.

<sup>390</sup> CA Versailles, 29 October 1992, LawLex025949.



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Providing partial<sup>391</sup>, inaccurate<sup>392</sup> or non up-to-date<sup>393</sup> information on the network and its development prospects<sup>394</sup>, on the very existence of the network<sup>395</sup> or on the state and prospects of the local market<sup>396</sup>, on the competition on the same territory by wholesalers of the brand's products who are provided with training and the know-how from the network<sup>397</sup>, or concealing the bankruptcy of a previous franchisee on the same area<sup>398</sup>, the large number of franchisees within the network<sup>399</sup>, the rapid turnover of member undertakings<sup>400</sup>, the level of monthly contributions<sup>401</sup>, or the fact that the franchisor is prohibited from managing a business<sup>402</sup>, characterize fraudulent non-disclosure. Concealed or omitted events must however pre-exist the formation of the contract<sup>403</sup> or have been reasonably foreseeable<sup>404</sup>.

The courts were initially highly favorable to franchisees in actions for annulment but now appear to be returning to a stricter assessment of vitiated consent by requiring franchisees to clearly establish that the omission of the alleged elements was decisive to their consent<sup>405</sup> or that the franchisor knowingly provided incorrect data<sup>406</sup>. A franchisee is also precluded from claiming that the state of the local market was essential and decisive when, having taken over a business in the knowledge that it would have to be

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<sup>391</sup> CA Lyon, 28 March 1997, LawLex025656, 31 March 2005, LawLex06264: lack of handing over of virtually all information required by Article L. 330-3 and Article R. 330-1 of the Commercial Code; CA Toulouse, 13 September 2000, LawLex025318.

<sup>392</sup> CA Paris, 26 January 2001, LawLex024682.

<sup>393</sup> CA Aix-en-Provence, 4 May 2006, LawLex061836; CA Paris, 23 June 2006, LawLex07165.

<sup>394</sup> CA Rennes, 24 January 1996, LawLex025530 approved by Cass. com., 24 March 1998, LawLex025112; CA Caen, 3 November 2005, LawLex06389; CA Aix-en-Provence, 13 December 2012, LawLex1310: failure to provide information relating to the results and to the operation of the network, which would have deterred the candidate from contracting and from experiencing commercial failure; CA Paris, 16 November 2016, LawLex161971: franchisor having concealed the recent liquidation of a franchisee as well as the presence in the area conceded to the franchisee of depositaries with the same benefits as the franchisees and therefore likely to be in active competition with them.&#10;

<sup>395</sup> CA Poitiers, 11 March 1997, LawLex025650; CA Paris, 17 March 2010, LawLex101345, on the failure by the franchisor to give the dates of the conclusion of contracts concluded with other franchisees and the concealment of its previous failures.

<sup>396</sup> CA Lyon, 8 January 2004, LawLex041514; CA Paris, 16 November 2016, LawLex161971: presentation of the local market based on old data and which conceals the presence of four depositaries of the brand.

<sup>397</sup> Cass. com., 13 June 2018, LawLex18949.

<sup>398</sup> TGI Avignon, 9 December 2003, LawLex041173; Cass. 1re civ., 3 November 2016, LawLex161805,

<sup>399</sup> CA Paris, 8 April 2004, LawLex091648; 26 October 2006, LawLex07759: concealment of the number of franchisees having left the network in the last twelve months; 22 May 2008, LawLex082196: incomplete, erroneous or ambiguous information, particularly concerning the number of network members. Cf. CA Dijon, 8 April 2010, LawLex10594, holding that the lack of information on the withdrawing members has not vitiated the franchisee's consent who does not establish that this was a decisive element for it and where there are clearly more incoming members than withdrawing ones.

<sup>400</sup> CA Colmar, 30 September 2015, LawLex151264; CA Paris, 17 January 2018, LawLex18142.

<sup>401</sup> CA Paris, 13 June 2007, LawLex09889.

<sup>402</sup> CA Paris, 3 December 1999, LawLex025260.

<sup>403</sup> CA Aix-en-Provence, 28 September 2017, LawLex171650.

<sup>404</sup> CA Orléans, 26 October 2017, LawLex171777; 6 December 2017, LawLex172081.

<sup>405</sup> See in particular Cass. com., 5 January 2016, LawLex1650, rejecting nullity of the contract where the franchisee could not demonstrate that the concealment of the extent of personal bankruptcy of the franchisor and the fact that he had been barred several years earlier from managing a business were decisive factors vitiating his consent; CA Paris, 20 January 2016, LawLex16187. Also see CA Paris, 19 April 2017, LawLex17738, finding that minor errors in the pre-contractual information document on the presence of a member of the network which has since disappeared or on an activity which represents only 10% of sales are not likely to have been decisive to the candidate's consent and CA, Paris, 6 December 2017, LawLex172081.

<sup>406</sup> CA Paris, 16 December 2015, LawLex151825; CA Paris, 20 January 2016, cited above.



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revitalized, he did not carry out market research for the area in question<sup>407</sup>. Similarly, the franchisee who cannot show that the age of franchisor's creation or the latter's solvency were clearly decisive factors in its decision to contract, may not subsequently claim fraud in respect thereof at the conclusion of the contract<sup>408</sup>. Also, the failure by the franchisor to inform the candidate about the transfer of its charges to a third party organization does not vitiate consent when it has not been shown that it has had an impact on the franchisor's accounts to the extent that it could conceal the latter's deficit or alter its image to the extent that the franchisee would not have contracted<sup>409</sup>.

### Section 4 Performance of contract

#### **I. Rights and obligations of franchisor**

##### A. Transmission of know-how

#### **6.58. Tested know-how.**

Franchising implies the reiteration of a successful undertaking and therefore the existence of a previous, valid, viable and verifiable success. The system conceived by the franchisor must have been put into practice, tested and tried to be validly transmitted to franchisees. The franchise agreement may be cancelled for lack of cause if the know-how transmitted by the franchisor has not been tested before the network was created<sup>410</sup>.

Experimentation is assessed in concreto. It may result from the long tradition and certain know-how of the franchisor in the relevant area<sup>411</sup>. In certain service franchises, experience obtained by the franchisor may even supplement the lack of originality of the transmitted know-how<sup>412</sup>. Experience obtained abroad may be claimed by the franchisor<sup>413</sup>, even if the transposition in France of know-how has subsequently given rise to failure by reason of the market context<sup>414</sup>. In turn, know-how which has proven its worth in France is validly transmitted to a franchisee who proposes to implement it in the USA, even if the franchisor has not tested it abroad as part of a pilot plant<sup>415</sup>. Failure to develop the

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<sup>407</sup> Cass. com., 5 January 2016, LawLex1631.

<sup>408</sup> CA Paris, 3 May 2017, LawLex17855.

<sup>409</sup> CA Versailles, 27 March 2018, LawLex18514.

<sup>410</sup> Cass. com., 30 January 1996, LawLex024343, approving CA Bordeaux, 8 February 1994, LawLex025371.

<sup>411</sup> Cass. com., 24 May 1994, LawLex021564; CA Paris, 26 March 1992, LawLex021743.

<sup>412</sup> CA Paris, 16 April 1991, LawLex025841: although the lack of originality of know-how is irrelevant in some service franchises, experience obtained by the franchisor is essential.

<sup>413</sup> CA Paris, 27 May 1993, LawLex026006.

<sup>414</sup> Cass. com., 13 December 1994, LawLex024352, approving CA Paris, 29 May 1992, LawLex025925.

<sup>415</sup> CA Versailles, 27 May 1993, LawLex026005.



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network also does not justify the cancellation of the agreement where it causes no prejudice to the franchisee, who has seen his turnover considerably increase in the contract period<sup>416</sup>. Lastly, the franchise is not void for absence of cause solely because it was set up only a few months before the signing of the franchise agreement where its founders had previously acquired solid experience individually and this experience has served as a basis for the franchised concept<sup>417</sup>.

Must know-how be tested in a pilot plant<sup>418</sup>? This requirement, laid down by the AFNOR Z 20-000 standard of August 1987 adds a condition to the European provisions which only provide for testing by the franchisor<sup>419</sup>. Some decisions however claim that know-how should have previously been tested by third parties<sup>420</sup> or that there should already be a commercial network on the date of conclusion of the contract<sup>421</sup>. **Others have held that the operation of a pilot site at the beginning and then throughout the existence of the network does not constitute a legal obligation for the franchisor, who must only have successfully tried and tested its know-how<sup>422</sup>.** Where the franchisee knew that he/she was to be the first representative of the brand<sup>423</sup>, has accepted to serve as a pilot plant<sup>424</sup> or knew that the pilot plant had only operated for six months before having committed himself<sup>425</sup>, the non-development of the network cannot justify the annulment of the franchise agreement. **Thus, a franchisee cannot successfully claim that the franchisor concealed that its site was one of the first tests in the provinces of a tried and tested concept in the Parisian region when, for that very reason, it obtained an exemption from payment of the franchise entry and the national marketing fee<sup>426</sup>.** Similarly, a franchisor having more than twenty years experience in the field can set up a franchise network without necessarily having tested its know-how within a pilot plant<sup>427</sup>.

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<sup>416</sup> CA Rennes, 22 April 2014, LawLex141976.

<sup>417</sup> CA Aix-en-Provence, 12 January 2011, LawLex11124.

<sup>418</sup> After being discovered by the franchisor, know-how may be tested within pilot plants in order to determine whether its effects may be reproduced on a wider scale. This experimentation is frequently made according to the three/two rule, i.e. within three pilot plants for a two-year period.

<sup>419</sup> Article 1(1)(g) of Regulation No 330/2010 of 20 April 2010 defines know-how as "a package of non-patented practical information, resulting from experience and testing by the supplier".

<sup>420</sup> CA Lyon, 30 May 1997, LawLex025675: a franchise contract is null and void where the transmitted know-how has not been tested by pilot plants.

<sup>421</sup> Cass. com., 10 May 1994, LawLex024357: the non-existence of any commercial network on the date of conclusion of the franchise contract establishes the lack of prior experimentation of the franchisor's know-how.

<sup>422</sup> CA Paris, 24 April 2017, LawLex17826; 28 February 2018, LawLex18372. See also Cass. com., 8 June 2017, LawLex171023, considering that the absence of pilot site does not justify the cancellation of the contract if the franchisor has organized training sessions during which it transmitted a specific know-how to the franchisee.

<sup>423</sup> CA Paris, 29 May 1991, LawLex025848: a franchise contract cannot be cancelled for lack of network development where the franchisee did not know that it was the first representative of the brand on the date of conclusion of the contract.

<sup>424</sup> CA Rouen, 14 May 1992, LawLex025918; T. com. Paris, 5 November 2002, LawLex043490.

<sup>425</sup> CA Lyon, 27 February 2014, LawLex141625; see also CA Lyon, 7 November 2013, LawLex131613.

<sup>426</sup> CA Paris, 10 May 2017, LawLex17876.

<sup>427</sup> CA Paris, 2 March 2016, LawLex16493.



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The lack of tested know-how can cause the the contract to be voided for lack of cause<sup>428</sup> or vitiated consent<sup>429</sup>.<sup>430</sup> He cannot however claim a deception was perpetrated in order to have the contract voided for lack of know-how through experience where he knew that the network, of American origin, only existed in an embryonic stage in France and that he would have to assess the potential of adapting it to the French market himself. The franchisee may also obtain the termination of the contract due to the franchisor's fault where that franchisor does not constitute a true network<sup>431</sup>.

### B. Duty of assistance

#### **6.64. Duty to advise.**

Technical assistance owed by the supplier is coupled with an obligation to provide advice, which must result in positive acts: recommendations, notice and indications. Thus, the franchisor must inform the franchisee, even if he/she is experienced, of any technical difficulties related to an installation<sup>432</sup>, **and also dissuade it from leasing premises that are unsuitable due to their location, size and the cost of rent being liable to prevent the franchisee from achieving a minimum rate of return**<sup>433</sup>. The franchisor breaches his obligation to provide advice where, having taken payment for a location survey, he offers no alternative solution to the franchisee subject to a municipal by-law prohibiting retail sales from the premises rented for that purpose<sup>434</sup>. On the other hand, when the contract does not include such an obligation, the choice of a location offering limited potential cannot be attributed to the franchisor<sup>435</sup>. As a mere best-effort undertaking, the advice obligation is fulfilled where the franchisor makes various suggestions and proposals intended to improve the profitability of the business<sup>436</sup>, the presentation of products in the store, the management of stocks and purchases, and profits<sup>437</sup>.

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<sup>428</sup> CA Aix-en-Provence, 4 March 1992, LawLex025901 upheld by Cass. com., 10 May 1994, LawLex024357; CA Paris, 11 June 1992, LawLex025928; CA Bordeaux, 8 February 1994, LawLex025371 upheld by Cass. com., 30 January 1996, LawLex024343.

<sup>429</sup> CA Versailles, 29 October 1992, LawLex025949; CA Bordeaux, 15 March 2000, LawLex025290; CA Paris, 8 November 2001, LawLex024613.

<sup>430</sup> CA Lyon, 11 April 2013, LawLex13699.

<sup>431</sup> CA Paris, 15 October 1998, LawLex025143. Cf. Cass. com., 24 May 1994, LawLex021564, upholding that a contract cannot be terminated for lack of previous experience of the franchisor where the latter is the heir to a long tradition in the relevant area and it own certain know-how regarding the sale of the contract goods.

<sup>432</sup> Cass. com., 8 January 2002, LawLex024969; CA Rouen, 24 October 2013, LawLex131518.

<sup>433</sup> CA Paris, 23 May 2018, LawLex18799.

<sup>434</sup> Cass. com., 28 September 2010, LawLex101059.

<sup>435</sup> CA Toulouse, 14 October 2015, LawLex151358.

<sup>436</sup> CA Paris, 31 January 2002, LawLex024698.

<sup>437</sup> CA Poitiers, 29 November 2011, LawLex112014.



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However, the franchisor's advice and assistance duty is limited by the independence of the franchisee's undertaking<sup>438</sup>. Thus, the franchisor is not required to assist the franchisee when transferring its business, even when the contract provides for its prior consent<sup>439</sup>. **The franchisor's duty to assist does not require him to accept the placing into lease-management of the business or to find a buyer for the franchisee**<sup>440</sup>. Since the franchisor must not interfere in the franchisee's management, it cannot be blamed for having failed to comply with its assistance duty where that duty has not been requested<sup>441</sup>. Similarly, a more rigorous trend in the case law finds courts ruling that the failure to provide assistance cannot be deduced merely due to the financial difficulties encountered by the franchisee, who remains an independent trader responsible for its own management<sup>442</sup>.

### **6.64\_01. Assistance in the event of financial difficulties.**

**In spite of the strong integration of franchise networks, franchisees are independent traders and bear the financial risks inherent to their activity. The courts therefore consider that the franchisor is not required, under the duty of assistance, to provide any particular financial or advertising support to a franchisee encountering significant cash-flow problems<sup>443</sup>, bail it out<sup>444</sup>, take a stake in its capital<sup>445</sup> or to take over the operations of franchisees due to deficits<sup>446</sup>.**

**Likewise, the assistance duty does not give rise to any obligation to renegotiate, reduce or amend contractual provisions. The franchisor is therefore not bound to waive the financial clauses of the contract, even where the franchisee is the victim of an incident which affects the functioning of its store<sup>447</sup>. Unless otherwise provided for, the franchisor has no duty to redefine a financial plan on behalf of its franchisee in difficulty, or to encourage it to cease its exploitation<sup>448</sup>. Some decisions have however excessively extended the scope of application of the franchisor's advice duty to the recommendation of**

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<sup>438</sup> CA Orléans, 8 September 1997, LawLex025038; CA Douai, 6 February 2003, LawLex04428: franchisees operate an undertaking in their name and must bear the burdens of any contractor where the franchisor has provided assistance; CA Lyon, 12 June 2014, LawLex142130; see also CA Paris, 24 April 2013, LawLex13810: a franchisee cannot claim a breach on the part of the franchisor of his duty to provide assistance where the latter has proposed some measures to resolve the difficulties encountered which were not followed up, insofar as a franchisee is not immune to all the risks inherent to a business activity.

<sup>439</sup> CA Lyon, 8 January 2004, LawLex041514.

<sup>440</sup> CA Versailles, 10 October 2017, LawLex171703.

<sup>441</sup> CA Paris, 16 November 2011, LawLex111848.

<sup>442</sup> CA Paris, 2 December 2015, LawLex151656; 16 December 2015, LawLex151825; 20 January 2016, LawLex16187; 2 March 2016, LawLex16496.

<sup>443</sup> CA Rennes, 3 July 2012, LawLex121628.

<sup>444</sup> CA Paris, 19 April 2017, LawLex17738.

<sup>445</sup> CA Toulouse, 14 October 2015, LawLex151358

<sup>446</sup> Cass. com., 7 January 2014, LawLex143.

<sup>447</sup> CA Paris, 14 January 2004, LawLex041547.

<sup>448</sup> Cass. com., 17 May 2005, LawLex07155, quashing on this issue CA Paris, 3 December 2003, LawLex07216; CA Paris, 6 June 2018, LawLex18883.



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measures such as allowing the franchisee to correct its situation<sup>449</sup>, if necessary by amending components of the franchise which seem inappropriate<sup>450</sup>. Thus, in a questionable ruling establishing by anticipation the unforeseeability mechanism introduced by the ordinance for the reform of contract law, the Court of Cassation held that a franchisor, who is bound under the obligations arising from the contract by a duty of close and loyal cooperation, must, if the intended development plan proves difficult to achieve, negotiate with the franchisee and propose acceptable terms<sup>451</sup>. Later, while acknowledging that the franchisor has no obligation to compensate the franchisee for its loss of earnings or ensure the recovery of its business, the Paris Court of Appeal confirmed the trend started by the Court of Cassation in considering that the franchisor's liability may be incurred due to the conspicuous bad faith shown in stubbornly refusing to help the franchisee to overcome the difficulties that the franchisor had itself partly created, notably through the practice of charging discriminatory prices compared to other members of the network<sup>452</sup>.

## II. Rights and obligations of franchisee

### 6.87. Royalties.

While the entry fee is owed by the franchisee to the franchisor at the time of the formation of the contract, the franchisor receives the royalty as remuneration throughout the contractual relationship. Such a royalty always exists in service franchise contracts; its inclusion in distribution franchise contracts is not permanent where the franchisor may be paid via the price of the goods or because it bills on behalf of the franchisees<sup>453</sup>. The royalty covers several services provided by the franchisor: advertising costs<sup>454</sup>, brand availability, technical and commercial assistance, etc<sup>455</sup>. Its existence is essential since it allows a proper commercial and technical functioning of the network, guarantees the profit of the franchisor and the franchisee and may fund an R&D budget.

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<sup>449</sup> Cass. com., 5 December 2000, LawLex03775.

<sup>450</sup> CA Douai, 6 September 2007, LawLex071744.

<sup>451</sup> Cass. com., 15 March 2017, LawLex17539, upholding CA Paris, 7 January 2015, LawLex1525. Contra, CA Paris, 26 April 2017, LawLex17826, according to which in the absence of bad faith on the part of the franchisor, a change in economic conditions and regulations for the exercise of the franchised activity does not trigger any duty to renegotiate.

<sup>452</sup> CA Paris, 27 September 2017, LawLex171582.

<sup>453</sup> Cass. com., 23 June 2004, LawLex041669; 30 June 2004, LawLex041665.

<sup>454</sup> Cass. com., 16 June 1992, LawLex024419.

<sup>455</sup> CA Riom, 10 February 2016, LawLex16356, holding that, regardless of whether or not it was actually transferred, the royalties owed by the franchisee are not exclusively based on the know-how of the franchisor but also on the right to exploit the trade mark, on commercial terms and conditions and the training given.



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The basis and terms of payment of the royalty are fixed by the contract. The franchisee cannot rely on the fact that the drafting of the contract is ambiguous to try to avoid its obligations<sup>456</sup>. Moreover, the franchisor does not commit a fault by charging a royalty where it does not exceed the percentage mentioned in the provisional operating account or the scale rate included in the franchise contract<sup>457</sup>. The royalty is generally established in three different ways: a fixed lump sum, an individual fixed sum for each of the franchisee's contract with its customers or a sum proportional to the turnover. The latter is the most usual and is often degressive in order to favor the franchisees' development. In such case, the franchisee's duty to pay the royalty goes hand in hand with the obligation to declare its monthly turnover and the failure to respect either of those obligations gives rise to the termination of the contract<sup>458</sup>. **Thus where the franchisee deliberately grossly underestimates his turnover (- 136%)<sup>459</sup>, or despite reminders, fails to provide to the franchisor its yearly balance sheets on which the royalty is based<sup>460</sup>, he is guilty of a serious breach justifying the immediate termination of the relationship by the franchisor. Furthermore, where, despite the fact that a clause of the franchise agreement stipulates an audit of the franchisee's accounts, the franchisee refuses an audit to verify its declared turnover, which is the basis for the calculation of fees, the franchisor has a personal interest in demanding actual performance of that provision<sup>461</sup>.** On the other hand, failing to declare certain benefits is not necessarily a result of the franchisee's intention to hide its turnover, but can be because they are non-billable benefits<sup>462</sup>.

The payment of the royalty is a substantial obligation of the franchisee. A franchise agreement is a bilateral contract with mutual obligations for the parties: the franchisee's obligation is to pay the royalty in consideration for the franchisor's services<sup>463</sup>. The franchisee may release itself from paying the royalty only where the franchisor fails to comply with its obligations. The implementation of the exception of non-performance is however subject to strict conditions. The franchisor's default must be serious and relate to a material obligation<sup>464</sup>, such as the duty of assistance<sup>465</sup> or the exclusivity obligation<sup>466</sup>. The franchisee must establish that the alleged non-performance is real, as well as the fact that it is prior or

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<sup>456</sup> Cass. com., 20 March 2007, LawLex07259, approving CA Paris, 8 December 2004, LawLex07416.

<sup>457</sup> Cass. com., 13 February 2001, LawLex020086, approving CA Douai, 19 March 1998, LawLex020087.

<sup>458</sup> CA Paris, 28 September 2011, LawLex111616.

<sup>459</sup> CA Paris, 28 January 2015, LawLex15125.

<sup>460</sup> CA Versailles, 21 February 2017, LawLex17452.

<sup>461</sup> CA Paris, 26 October 2017, LawLex171754.

<sup>462</sup> Cass. com., 30 March 2016, LawLex16710.

<sup>463</sup> CA Paris, 22 September 1992, LawLex021711.

<sup>464</sup> Cass. com., 7 February 1995, LawLex021488; CA Paris, 19 March 2014, LawLex141746.

<sup>465</sup> CA Aix-en-Provence, 24 September 1998, LawLex025141; Cass. com., 13 June 2018, LawLex18948.&#10;

<sup>466</sup> CA Grenoble, 19 February 1997, LawLex021292: a franchisee may suspend the payment of its fees where the franchisor breaches its exclusivity obligation.



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simultaneous to the suspension of payments<sup>467</sup>. Such is not the case where the franchisee purports to justify its failure to pay due to the franchisor's non-performance of its obligation to supply translation software whereas there was no specified time period for the provision of the software and its provision did not appear to be essential to the contract insofar as the franchisee had waited two years before signing the contract concerning the terms of its implementation<sup>468</sup>. **The franchisee also cannot, in order to justify the non-payment of its advertising royalties, claim that commercial assistance from the franchisor has ceased insofar as that assistance was not contractual and had no link to the non-performed obligation<sup>469</sup>.** The court may only hold both parties responsible for the termination where the existence of the defaults is established but not the chronology<sup>470</sup>. A franchisee cannot claim that the royalty is manifestly disproportionate to the service rendered by the franchisor where the claim is only based on a single non-representative service out of all those from which he benefits<sup>471</sup>. In order to be able to rely on an anticipatory breach defense, the franchisee must have sent a formal letter to the franchisor demanding compliance with its obligations<sup>472</sup>.

In addition, a franchisee cannot compel the franchisor to renegotiate the amount of royalties by invoking the disruption of the balance of the contract caused by events that were not stipulated as essential conditions for its conclusion, or the decline of its turnover, when the royalties are contractually unrelated to its financial results<sup>473</sup>.

The non-payment by the franchisee of its royalties is a serious ground for termination of the franchise contract<sup>474</sup>. In practice, as a precaution, the termination of the contract will be preceded by one or more letters of formal notice to comply<sup>475</sup>. The termination will be held against the franchisee who persists in failing to pay<sup>476</sup>. **Lastly, the franchisor is not deemed to have definitively waived payment of the franchise fee merely because the franchisee was not required to pay that fee during the start-up period<sup>477</sup>.**

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<sup>467</sup> Cass. com., 25 January 2000, LawLex020852; Paris, 27 February 2013, LawLex13263JB; CA Montpellier, 10 December 2013, LawLex131887; CA Versailles, 6 May 2014, LawLex141999.

<sup>468</sup> Cass. com., 27 April 2011, LawLex11856.

<sup>469</sup> CA Paris, 22 November 2017, LawLex171946.

<sup>470</sup> CA Paris, 16 June 1993, LawLex022654.

<sup>471</sup> CA Paris, 28 November 2012, LawLex122396.

<sup>472</sup> CA Paris, 9 January 2014, LawLex1424.

<sup>473</sup> CA Paris, 15 June 2016, LawLex161132.

<sup>474</sup> CA Paris, 11 March 1988, LawLex022649; Cass. com., 16 January 1990, LawLex025766; CA Montpellier, 10 December 2013, LawLex131887.

<sup>475</sup> Cass. com., 11 January 2000, LawLex024382; 6 April 1999, LawLex024393; CA Rennes, 25 June 1997, LawLex025026; CA Paris, 8 December 1999, LawLex025262.

<sup>476</sup> T. com. Marseille, 29 April 1999, LawLex025206; CA Paris, 21 May 1999, LawLex025216; 27 May 1993, LawLex026006.

<sup>477</sup> CA Aix-en-Provence, 28 September 2017, LawLex171650.



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### 6.89. Intuitus personae.

The introduction of an element of *intuitus personae* in distribution contracts concluded between legal entities is common. Of course, tying the fate of a contract concluded with a company to the person of its top executive(s) or to the formation of its capital results in lifting the corporate veil. However, the principle of contractual freedom advocates the recognition of *intuitus personae* clauses. These clauses are of great interest for the franchisor as they guarantee the confidentiality of know-how and the continuity of its sale structures. Thus, a franchise agreement concluded *intuitu personae* must be terminated where the franchised company opens up its capital to a company competing with the franchisor's company<sup>478</sup>. Likewise, the assignment of 95% of the shares in a franchised company to a competing group amounts to a transfer of franchise contract and may be grounds for termination<sup>479</sup>. **A hamburger chain franchisee which acquires a share in a restaurant belonging to a chain of pizzerias violates the clause prohibiting any investments in the fast food sector, even if the products are not identical and the restaurants are 33 km apart from each other, insofar as the two businesses share the same basic characteristics (practically immediate service, low-price products, limited and standardized menus, extensive opening hours etc.)<sup>480</sup>. In a contract concluded *intuitu personae* providing for automatic termination without notice in the event of impossibility for the other party to personally perform the service, in particular due to any conviction related to his business activity or due to facts liable to harm his reputation, it was held that the indictment of the interested party for corruption with regard to the staff of an essential client of the brand was, despite the presumption of innocence, detrimental to his reputation and justified the immediate termination as provided for in the contract<sup>481</sup>. In addition, even if the franchise agreement does not contain a non-compete clause applicable to the contract period, the *intuitus personae* which governed its conclusion and the principle of good faith in the performance of the contract precludes the franchisee from opening a competing restaurant through a third-party undertaking<sup>482</sup>. The courts have also found that where the manager of a franchisee participates in the creation and organization of an association for the defense of the interests of network members, the object of which demonstrates a clear mistrust with respect to the franchisor, he is in breach**

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<sup>478</sup> CA Paris, 6 February 1992, LawLex025893; 3 July 1998, LawLex021099.

<sup>479</sup> Cass. com., 15 January 1991, LawLex024436, upholding CA Orléans, 28 February 1989, LawLex02000101.

<sup>480</sup> CA Paris, 13 December 2017, LawLex172085.

<sup>481</sup> Cass. com., 8 December 2015, LawLex151789.

<sup>482</sup> CA Paris, 15 February 2017, LawLex17354.



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of an essential obligation of the franchise agreement, concluded *intuitu personae*, justifying the implementation of the termination clause for “breach seriously affecting the franchisor’s interests”<sup>483</sup>.

### 6.90. Ownership of goodwill.

Can a franchisee who carries out its activity in premises which it rents claim ownership of the goodwill pursuant to Articles L. 145-4 et seq. of the Commercial Code on commercial leases? The recognition of goodwill ownership allows the trader who is a lessee to obtain the renewal of its lease upon expiry or, failing any renewal, to obtain compensation for the injury caused to it by the deprivation of premises devoted to the exploitation of its business. Goodwill ownership is justified only if the lessee has accumulated customers in the leased premises.

Initially, the Court of Appeal of Paris denied franchisees the ownership of their clientele on the grounds that customers are principally attracted by the franchisor's brand<sup>484</sup>. It was therefore for the franchisee, if it wanted to benefit from the commercial leases status, to establish that it had its own clientele which was distinct from the franchisor's<sup>485</sup>, by showing that its rights in the lease attracted the clientele more than the franchisor's brand<sup>486</sup>. Only one isolated decision in 1992 asserted that the franchisee whose contributions managed to make material the franchisor's mainly virtual clientele was entitled to the renewal of its commercial lease<sup>487</sup>. The Court of Appeal then reversed the case law and considered that the franchisee, as an independent trader, is as such the owner of its clientele<sup>488</sup>. This solution has subsequently been established by the Court of Cassation<sup>489</sup>: “the clientele is itself part of the franchisee's business since, even if it is not the owner of the brand and of the sign made available to it during the performance of the franchise contract, it is created by its activity, with resources that it implements at its own risks as it enters into contracts in a personal capacity with its suppliers or money lenders”. The corporate risk becomes the major criterion of the goodwill ownership. The clause requiring the franchisee to operate its activity only under the franchisor's sign is null and void where it undermines the partial non-specialization of the commercial lease<sup>490</sup>. Thus, where the franchisor is also the

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<sup>483</sup> CA Paris, 3 May 2017, LawLex17855.

<sup>484</sup> CA Paris, 6 February 1996, LawLex025334; approving TGI Évry, 9 December 1993, LawLex025359.

<sup>485</sup> TGI Paris, 30 October 1998, LawLex025150: the benefit of the commercial lease status is subject to the franchisee bringing evidence that it has a specific clientele, attracted by its personal activity, or even by the location of the premises, and not only by the franchisor's brand.

<sup>486</sup> TGI Paris, 26 September 1995, LawLex025491: a franchisee must be regarded as the owner of its business where it holds a group of rights having an attractive power on customers and the franchisor's brand is only one element among others.

<sup>487</sup> TGI Paris, 24 November 1992, LawLex025957.

<sup>488</sup> CA Paris, 4 October 2000, LawLex025323 and LawLex02000246; CA Toulouse, 13 January 2000, LawLex025269; CA Paris, 3 July 2002, LawLex024312, confirming the solution.

<sup>489</sup> Cass. 3e civ., 27 March 2002, LawLex024694.

<sup>490</sup> Cass. 3e civ., 12 July 2000, LawLex024732, approving CA Caen, 8 September 1998, LawLex024733.



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franchisee's lessor and the lease is exclusively devoted to the franchised activity, the termination of the distribution agreement does not result in the termination of the lease and does not require the supplier to pay compensation for notice where it is possible for the franchisee to claim non-specialization<sup>491</sup>.

The franchisee is therefore entitled to compensation for exclusion in case of refused renewal where the local clientele exists because of its activity and is part of the business it operates at its own risks<sup>492</sup>. On the other hand, the existence of a local clientele attached to the franchisee's business does not mean that the franchisor could not also have developed a national clientele attached to the reputation of his trade mark and he may, without being guilty of unfair competition, solicit customers on the client list he has built at the term of the contract and direct them towards the new franchisee<sup>493</sup>. After initially considering that the franchisee was entitled to damages for compensation of the injury that is caused by the termination of the contract and the existence of a non-compete clause which dispossesses it from its clientele<sup>494</sup>, the Court of Cassation reversed its position. It excluded the application of the rules on unjust enrichment to the franchisee claiming to be dispossessed of its clientele because of the effect of a post-contract non-compete clause, insofar as the cause of enrichment and impoverishment, according to the Court, rests in the performance or termination of the contract<sup>495</sup>. The franchisee may certainly not claim a goodwill indemnity when the franchisor has waived the right to assert the non-affiliation and non-compete obligation<sup>496</sup>. **However, where the customers are the franchisee's property under the franchise agreement, the franchisor who replaces the operating software by a new tool that allows him to disable the franchisee's account on expiry of the contract thus depriving the latter of access to those customers, incurs the termination of the contract for fault<sup>497</sup>. Likewise, a clause in a rider to a franchise agreement stipulating that it takes precedence over the contract itself and which gives the franchisee ownership of the local clientele precludes the transfer to the franchisor of ongoing contracts at the date of the termination, laid down in another provision of the contract<sup>498</sup>, or the application of a post-contractual non-compete clause which deprives it of the right to exploit that clientele<sup>499</sup>. Lastly, the purchaser of the franchisee's business who is not a member of the network cannot reproach the franchisor for using**

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<sup>491</sup> Cass. 3e civ., 30 June 2010, LawLex10800.

<sup>492</sup> Cass. 3e civ., 27 March 2002, LawLex024694.

<sup>493</sup> CA Rennes, 28 June 2011, LawLex111299. But see CA Paris, 29 April 2014, LawLex14672, considering that contractual clauses and mechanisms allowing the franchisor to obtain disclosure of the client lists by franchisee infringes the goodwill ownership rights of the latter.

<sup>494</sup> Cass. com., 9 October 2007, LawLex071569.

<sup>495</sup> Cass. com., 23 October 2012, LawLex122236.

<sup>496</sup> CA Angers, 17 February 2015, LawLex15236.

<sup>497</sup> CA Paris, 10 May 2017, LawLex17871.

<sup>498</sup> CA Paris, 7 June 2017, LawLex171027.

<sup>499</sup> CA Paris, 13 December 2017, LawLex172064.



the seller's client list insofar as it is not included in the transferred property and its ownership is attached to membership of the network<sup>500</sup>.

The benefit of the goodwill ownership also results in the franchisee's fiscal independence<sup>501</sup>.

## Section 5 Termination of contract

### **III. Sudden termination of established commercial relationship**

#### **6.97. Application of Article L. 442-6, I, 5° of the Commercial Code to franchises.**

Like other distribution agreements, franchise agreements come under the scope of application of Article L. 442-6, I, 5° of the Commercial Code, which provides that: "any producer, commercial person manufacturer or person entered in the trades register is personally liable and obliged to compensate for any loss caused who [...] suddenly severs even partially an established commercial relationship without prior written notice which takes into account the length of the commercial relationship and respects the minimum period of prior notice established in accordance with business practices, by inter-trade agreements [...]. The above provisions do not take away the right to repudiate without prior notice in the event of non-fulfillment by the other party of his obligations or in the event of force majeure".

The provision applies to contractual relations whether or not formalized in writing and regardless of whether they are open-ended or fixed-term<sup>502</sup>. It does not however cover the situation where relations are maintained after the expiry of a non tacitly renewable fixed-term contract, such relations being precarious and able to end at any time, especially where the franchisor has not indicated that there was any possibility of renewal<sup>503</sup>. **The franchisee whose fixed-term contract is due to expire also cannot reasonably expect any pursuit of the commercial relationship in the future<sup>504</sup>. In the absence of evidence of a change in the contractual balance or a decline in profitability of the franchisee, the creation by the franchisor of three competing outlets on the catchment area of a distributor who has no contractual exclusivity does not constitute a breach of contract<sup>505</sup>.**

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<sup>500</sup> CA Agen, 13 June 2018, LawLex18914.

<sup>501</sup> CAA Paris, 3 October 2000, LawLex024979.

<sup>502</sup> CA Paris, 3 June 2011, LawLex111037: even if the parties have formally ruled out any tacit renewal.

<sup>503</sup> CA Paris, 14 October 2015, LawLex151322.

<sup>504</sup> Cass. com., 21 June 2017, LawLex171130. Also CA Paris, 28 February 2018, LawLex18372.

<sup>505</sup> CA Paris, 14 December 2016, LawLex1717.



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Even if the provision makes an exception for cases of non-performance of the contract, a franchisor cannot justify the sudden termination of relations for allegedly outstanding payments where the due date has not been reached at the time of the notification<sup>506</sup> or where their combined amount is only EUR 5 000<sup>507</sup>. On the other hand, an immediate termination of relations due to repeated outstanding payments by the franchisee does not incur the franchisor's liability especially when that measure is preceded by a number of reminders setting out the consequences of the failure to comply<sup>508</sup>. **Likewise, the violation of payment procedures put in place by the franchisor and the infringement of the image of the network constitute serious breaches justifying termination of the contract<sup>509</sup>.**

The notice period granted to the franchisee must take into account the reputation of the contract goods and allow him to redevelop his business activity in conditions capable of guaranteeing the maintenance of an equivalent level of business<sup>510</sup>. **However, belonging to even a very well-known network with a low market share does not constitute an obstacle to the franchisee's possibility to diversify<sup>511</sup>.** The existence of a situation of dependence, justifying an extension of the notice period may result from the accumulation of clauses imposed by the franchisor limiting the franchisee's ability to convert after the termination of the commercial relationship<sup>512</sup>. On the other hand, the franchisee who did not use the faculty available in the contract to obtain the franchisor's authorization to sell other products is not placed in a state of dependence when it has deliberately chosen to purchase exclusively from the franchisor<sup>513</sup>. Lastly, in assessing the adequacy of the notice period accorded in respect of trade conducted after the expiry of the contract, the courts must take account not of the relationship as a whole but only of the duration of the relations pursued post-contract<sup>514</sup>.

### IV. Consequences of the termination

#### A. Relations between the parties

##### 1° Franchisee

#### 6.99. Non-compete obligation.

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<sup>506</sup> CA Pau, 15 April 2010, LawLex10946.

<sup>507</sup> CA Lyon, 7 February 2013, LawLex1311.

<sup>508</sup> CA Paris, 16 November 2011, LawLex111848.

<sup>509</sup> CA Paris, 15 February 2017, LawLex17345.

<sup>510</sup> CA Rennes, 28 June 2011, LawLex111299.

<sup>511</sup> CA Paris, 22 November 2017, LawLex171946.

<sup>512</sup> CA Paris, 22 November 2017, LawLex171946.

<sup>513</sup> CA Paris, 22 November 2017, LawLex171946.

<sup>514</sup> CA Nimes, 5 May 2011, LawLex111049.



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Franchise agreements generally contain clauses providing for the post-contract relationship such as non-compete and non-reaffiliation clauses. Subject to fulfilling the conditions for validity<sup>515</sup>, which since the Macron Law of 6 August 2015 have become stricter, the franchisee is liable for the breach of such clauses.

### 1) Non-compete clause

There is violation of the non-compete clause where the franchisee continues the franchised activity within the same premises<sup>516</sup>, even if it adds a supplementary activity<sup>517</sup>, or within the same geographic area<sup>518</sup>, or uses a guarantee booklet for customers largely borrowing from his former franchisor's booklet<sup>519</sup>. The former franchisee also breaches the non-compete clause by proposing an offer which pursues similar objectives to those of the franchise and is directed towards a similar clientele, even if this is only one activity among many in his new business<sup>520</sup> or becomes involved with a company created by members of his family for the distribution of goods competing with those of the franchisor<sup>521</sup>. On the other hand, the fact that the franchisee assigns its business to two companies that are legally distinct but managed by the same person<sup>522</sup> or the fact that its lessee operates its business for a competing sign where the termination of the contract has released it from any obligation with respect to the franchisor<sup>523</sup> does not characterize a failure to comply with the non re-establishment obligation. Likewise, the director of a franchised company who is bound by the terms of the non-compete clause in the franchise agreement unless liability for those obligations has been expressly taken over by the company, does not breach his obligation solely because he has acquired a share in another franchised company where the latter company is located outside the geographical scope of application of the clause<sup>524</sup>. **Lastly, a non-compete clause which deprives the franchisee of the local customers that the franchisor has transferred to it in a rider to the contract is not enforceable**<sup>525</sup>.

### 2) Non-reaffiliation clause

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<sup>515</sup> Esp. paras. 0410, 0419, 0420 and 0481.

<sup>516</sup> CA Paris, 8 March 1996, LawLex04956; T. com. Paris, 19 December 1997, LawLex021198; CA Aix-en-Provence, 24 September 1998, LawLex025141.

<sup>517</sup> CA Paris, 23 November 2006, LawLex08390.

<sup>518</sup> CA Paris, 30 January 2002, LawLex03467.

<sup>519</sup> CA Nîmes, 27 June 1996, LawLex025584.

<sup>520</sup> CA Montpellier, 16 October 2012, LawLex122195.

<sup>521</sup> CA Aix-en-Provence, 7 March 2013, LawLex13376.

<sup>522</sup> Cass. com., 17 November 1998, LawLex021056, approving CA Paris, 8 March 1996, LawLex021978.

<sup>523</sup> CA Paris, 19 November 2009, LawLex10563.

<sup>524</sup> CA Toulouse, 11 May 2011, LawLex111059.

<sup>525</sup> CA Paris, 13 December 2017, LawLex172064.



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The fact that the franchisee exercises an activity under a sign or business name does not necessarily imply that it belongs to a network or a competing organization<sup>526</sup>. Furthermore, the breach of a clause that prohibits the franchisee from affixing on its store a nationally reputed business name is not manifest where it is not established that the new supplier has such a reputation<sup>527</sup>. Likewise, the creation of a new network by former franchisees is not wrongful where the clause only prevents the franchisee from becoming a member of a competing network<sup>528</sup>. The breach of the non-reaffiliation clause does not cause injury to the franchisor where the address and name of the franchisee have changed - in order to avoid any risk of confusion -, and he uses a new franchisor's standards and know-how<sup>529</sup>. On the other hand, a franchisee who becomes a member of a competing network<sup>530</sup> or creates its own network while being bound by an absolute prohibition from directly or indirectly participating in an organization comparable to the franchisor's one<sup>531</sup> fails to perform its non-reaffiliation obligation. In practice, a minority holding by the franchisor in the franchisee's business may be intended to make the distributor's re-affiliation to a competing network more difficult, especially where the franchisor has a veto right or a right of approval or maintains the holding after the transfer, thus complicating the management by the new supplier. It has been held that even in the absence of any exclusion clause, such exclusion could be ordered in application of the implicit intention of the parties, the impossibility of separating the holding and the distribution agreement and taking into consideration the usual practices in distribution networks<sup>532</sup>.

The conditions of lawfulness of a non-compete clause, which prohibits the franchisee from carrying out a similar or related activity to that of the franchise network he has left cannot be applied to non-reaffiliation clauses<sup>533</sup>. Neither is its validity subject to the stipulation of financial consideration<sup>534</sup>. However, a non-reaffiliation clause may not hinder the exercise of trade by the franchisee and must be proportionate to the franchisor's legitimate interests. **The purpose of the clause can, moreover, be the protection not only of franchisee teams, but also of branches and independent firms of the brand<sup>535</sup>. A clause prohibiting the franchisee from associating itself to a nationally or regionally-known chain and**

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<sup>526</sup> Cass. com., 8 July 2003, LawLex032735.

<sup>527</sup> Cass. com., 25 January 2000, LawLex024381, approving CA Versailles, 4 July 1997, LawLex025034. See also Cass. com., 20 May 2008, LawLex081088.

<sup>528</sup> CA Paris, 25 January 2006, LawLex08191.

<sup>529</sup> CA Paris, 28 April 2011, LawLex111248.

<sup>530</sup> CA Paris, 26 November 1999, LawLex020874.

<sup>531</sup> Cass. com., 4 April 1995, LawLex021467, quashing CA Poitiers, 19 May 1993, LawLex021641.

<sup>532</sup> Grenoble, 16 September 2010.

<sup>533</sup> Cass. com., 28 September 2010, LawLex101062.

<sup>534</sup> Cass. com., 31 January 2012, LawLex12248.

<sup>535</sup> CA Versailles, 21 February 2017, LawLex17428 and LawLex17452, upheld by Cass. com., 4 September 2018, LawLex181254.



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selling products of brands tied to that chains for a year and within a radius of five kilometers, is not proportionate to the legitimate interests of the franchisor and must be voided insofar as it deprives the franchisee of the support of a structured supply network making it impossible for him to continue the operation of his business under economically viable conditions<sup>536</sup>. Similarly, a non-reaffiliation clause is anticompetitive where the know-how it purports to protect is devoid of specific technical value, specificity and originality and its scope, both temporal (3 years) and geographical (5 km), is disproportionate to the objective pursued<sup>537</sup>. In order to establish the anticompetitive nature of a non-reaffiliation clause, the Paris Court of Appeal in addition requires that it appreciably restrict competition on the market concerned<sup>538</sup>. Even where the franchisee has continued to work with the franchisor after the termination of the franchise agreement, he is not bound by the non-reaffiliation clause in a contract which has not been expressly renewed<sup>539</sup>.

The franchisee's breach of the non-compete or non re-affiliation obligation incurs the payment of the penalty set out in the penalty clause of the contract<sup>540</sup>. The injury resulting from the breach of the non-compete clause cannot include the total loss of the clientele in a sector where the franchisees had been authorized under the contract to carry on a similar activity<sup>541</sup>. The franchisor cannot obtain as compensation the fees owed throughout the duration of the offense committed by the franchisee who has become a member of a competing network when it has taken no steps to operate or to franchise the sectors given up<sup>542</sup> or the margins that it would have been able to make until the end of the contract, especially when this would be several years later and the duration of the clause is limited to one year<sup>543</sup>.

### Section 6 Transfer of contract

#### **6.108. Right of preemption.**

Many franchise agreements give the franchisor a preemption right requiring the franchisees wishing to sell their business or shares therein to first offer the franchisor first refusal. Such clauses are often

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<sup>536</sup> Cass. com., 18 December 2012, LawLex122501.

<sup>537</sup> CA Paris, 6 March 2013, LawLex13350, upheld by Cass. com., 23 September 2014, LawLex14967, Ca Paris 3 April 2013, LawLex13516; upheld by Cass. com., 16 September 2014, LawLex14954; CA Paris, 11 September 2013, LawLex131325. Also see Cass. com., 8 June 2017, LawLex171021, declaring void a non-reaffiliation clause whose geographical scope is not identified in the absence of any definition of the catchment area.

<sup>538</sup> CA Paris, 2 July 2014, LawLex142187.

<sup>539</sup> CA Versailles, 30 January 2014, LawLex14240.

<sup>540</sup> CA Paris, 12 September 1997, LawLex025042.

<sup>541</sup> CA Paris, 18 December 1998, LawLex021031.

<sup>542</sup> CA Versailles, 11 May 2006, LawLex072015; contra CA Paris, 26 April 2017, LawLex17804.

<sup>543</sup> CA Saint-Denis de la Réunion, 4 May 2016, LawLex16943.



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associated with an option to purchase clause with the prices fixed by an independent expert or providing for a maximum buyback price in order to prevent evasions of the preemption right by the setting of prices which are abusively high. Such stipulations also have the object of preserving the coverage of the network and the franchisor's investments against destabilizing actions by competitors to destroy a competing network or to purchase it cheaply when the franchisor has made investments in terms of prospection and launching costs when building the network from scratch.

The legitimacy of preemption clauses is a subject of debate. The legislator attempted to place them within a legal framework at the time the LME law of 4 August 2008 was adopted. Article L. 442-6, II, e of the Commercial Code thus provides that clauses affording suppliers the possibility to obtain from a retailer any preferential right for the assignment or transfer of his business are null and void. The attempt has remained of no effect since the provision only refers to sales areas of less than 300 square meters and excludes contractual relations providing, directly or indirectly, trade mark or know-how licensing contracts. Stripped of any real content, the provision applies to practically no distribution agreement in force in virtually all types of networks regardless of sector with the exception of beer distribution contracts with small retailers (pubs), which in any case rarely stipulate a preemption right in the brewery's or the wholesaler's favor, as the wording of Article L. 442-6, II is moreover in contradiction with European law. The proposal for the strengthening of consumer rights, as adopted by the Senate in December 2011, before the change in the parliamentary majority, established a *per se* prohibition of all preferential rights for network leaders in the event of the transfer of an affiliated sales outlet, but that proposal was dropped in the context of the Hamon law on consumer protection which was ultimately adopted.

The Competition Authority has been rather critical in respect of preemption rights in food retail distribution contracts with franchisees<sup>544</sup>. It recommended the suppression of such rights in cases where the large retail group is not the owner of the store and has no financial stake in the company operating the business, but does accept the legitimacy of such rights where the network leader has been an actual partner in the development of the independent trader's business<sup>545</sup>. In its decision-making practice, the Authority has however opted for a much more moderate approach: it has upheld a preference clause in favor of a large retail chain in the food sector<sup>546</sup>, as well as a preemption clause of a distribution

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<sup>544</sup> Competition Authority Opinion No 10-A-26 of 7 December 2010 relative to affiliation contracts with independent stores and the terms for acquiring commercial property in the food retail sector.

<sup>545</sup> Competition Authority Opinion No 10-A-26 of 7 December 2010, pt 227.

<sup>546</sup> Competition Authority Decision No 11-D-20 of 16 December 2011, LawLex111949, limiting the preferential right to the duration of the contract.



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cooperative in the DIY sector in the case of the transfer of a franchise store on the grounds that all the clauses relating to the exit from the network (preemption, penalties etc.) did not produce any effect limiting the possibility for the stores to change their trade names<sup>547</sup>. The Court of Cassation, firstly ruled anticompetitive the stipulation of a right of preemption in favor of the franchisor, valid throughout the duration the term of the contract and one year after its term, as it limits the potential for competing distribution groups to buy independent stores<sup>548</sup>. Then, in the same case on referral, the Court of Cassation recognized that the priority right granted by the franchisee to its franchisor in the event of the divestiture of its business is not anticompetitive when it constitutes consideration for a solid commercial partnership with the latter, who is able to secure investments made, and where no evidence is brought to enable the court to measure in concreto, from an analysis of the market and of economic data, any possible artificial restriction of competition<sup>549</sup>.

The Macron Law of 6 August 2015<sup>550</sup> has adopted an intermediate position. Article L. 341-2 of the Commercial Code now deems automatically void ab initio or "unwritten" "any clause having as its effect, after the expiration or termination of one of the agreements referred to in Article L. 341-1, the restriction of the freedom to carry on his commercial activity of the trader having previously entered into this agreement". There is nevertheless provision for a derogation for the clauses which fulfill the four cumulative conditions inspired of Regulation No 330-2010 on vertical restraints. The clauses must relate to goods or services which compete with the contract goods or services; be limited to the premises and land from which the trader has operated during the contract period; be indispensable to protect the know-how, which is secret, substantial and identified, transferred by the supplier to the trader in the context of the contract; be of a duration not exceeding a period of one year after expiry termination of one of the agreement referred to in Article L. 341-1.

### I. Voluntary transfer

#### 6.110. Transfer by the franchisor.

Regarding franchising, *intuitus personae* can also concern the franchisor. In effect, the franchisee accepts obligations that are sometimes very restrictive only in consideration of for the qualities that it attributes to the franchisor's know-how.

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<sup>547</sup> Competition Authority Decision No 13-D-19 of 29 October 2013, LawLex131565.

<sup>548</sup> Cass. com., 4 November 2014, LawLex141238.

<sup>549</sup> Cass. com., 3 May 2018, LawLex18680.

<sup>550</sup> Law No 2015-990 of 6 August 2015 for the growth, activity and equality of economic opportunities.



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The courts consider that the acquisition of control by the franchisor does not constitute a cause of termination of the franchise agreement by the franchisee where it affects neither the continuation of the legal entity concerned<sup>551</sup>, nor the conditions of performance of the contract, since the franchisees are not deprived of the use of the brand and the know-how<sup>552</sup>. On the other hand, where the purchaser of the franchisor substantially amends the basic contractual conditions, the contract may be terminated against the franchisor<sup>553</sup>.

Although some judgments have considered that the transfer of its shares by the franchisor does not challenge the performance of the contract, where the *intuitus personae* is not required from the franchisor<sup>554</sup>, this is not the opinion of the Court of Cassation, which considers that the franchise agreement is concluded in consideration of the franchisor and, except with the franchisee's consent, cannot be transferred by result of the partial transfer of assets under a de-merger or by merger<sup>555</sup>. Thus, where the franchise network is transferred to a third party, without the transferee's consent, the franchisor is required to keep on performing its basic obligations until the end of the contract, without however being requested to organize a network identical to the network existing before the transfer<sup>556</sup>. Where the transfer has not been notified to the franchisee and his explicit consent has not been sought, the master franchisee to whom the franchisor has transferred the franchise agreement has no standing to bring proceedings for the payment of outstanding royalties<sup>557</sup>. Where a clause of the franchise agreement authorizes the transfer without the franchisee's consent, the transfer is unfairly implemented if the transferee, rather than continuing to perform the initial contract, proposes the signing of a new agreement under conditions which are clearly less favorable<sup>558</sup>. Likewise, where the activity may no longer be carried on because there is no trade mark, which is the essential component of the contract, the termination of the contract is attributable to the franchisor who has transferred the franchise agreement without the franchisee's consent<sup>559</sup>.

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<sup>551</sup> CA Paris, 23 November 2000, LawLex024680. Cf. CA Rennes, 20 January 2004, LawLex041608, which considers that the acquisition of the franchisor's control by a large perfumery group justifies the termination of the contract by the franchisees, where in the network in question, *intuitus personae* is bilateral.

<sup>552</sup> CA Paris, 11 January 2002, LawLex024627.

<sup>553</sup> CA Rouen, 9 November 2000, LawLex024690.

<sup>554</sup> CA Paris, 21 May 1999, LawLex025216; 2 April 2008, LawLex081157.

<sup>555</sup> Cass. com., 3 June 2008, LawLex08974 and LawLex08975; 24 November 2009, LawLex093558. See also CA Lyon, 11 June 2009, LawLex1022; Cass. com. 12 October 2010, LawLex101127; 19 March 2013, LawLex13448. See also CA Douai, 30 August 2018, LawLex181230.

<sup>556</sup> Cass. com., 28 June 2005, LawLex056748.

<sup>557</sup> Cass. com., 28 May 2013, LawLex13899.

<sup>558</sup> CA Dijon, 8 April 2010, LawLex10593 and LawLex10594.

<sup>559</sup> Cass. com., 31 January 2012, LawLex12186.



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On the other hand, the franchisee who has signed a contract providing for the possibility for the franchisor to transfer the franchise network without having to obtain the consent of its members, cannot subsequently reproach the latter for not having informed him of its plans<sup>560</sup>. Similarly, the takeover of the network by a competitor is not in itself a fault by the franchisor in respect of its members when the franchise agreement specifies that the *intuitus personae* of the contract relates only to the person of the franchisee<sup>561</sup>. Also the placing into lease-management of the franchisor's business is automatically enforceable against the franchisee when the franchise agreement contains a clause according to which the *intuitus personae* only concerns the person of the latter, who moreover undertakes to accept any changes in the person of the franchisor<sup>562</sup>. However, even when a clause of the franchise agreement authorizes a transfer without the consent of the franchisee, such a clause is implemented in bad faith if the transferee, instead of continuing to perform the initial contract, proposes the signing of a new agreement under much less favorable conditions<sup>563</sup>.

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<sup>560</sup> CA Paris, 10 May 2017, LawLex17876.

<sup>561</sup> CA Paris, 15 November 2017, LawLex171898.

<sup>562</sup> CA Paris, 7 March 2018, LawLex18393.

<sup>563</sup> CA Dijon, 8 April 2010, LawLex10593 and LawLex10594.



## CHAPTER 7

# COMMERCIAL AGENTS

### Section 2 General law on commercial agency

#### III. Performance of contract

##### A. Obligations of the agent

#### 7.30. Legal non-compete obligation.

Article L. 134-3 of the Commercial Code prevents the agent from representing a competing undertaking without his principal's agreement<sup>564</sup>. The scope of the non-compete clause applicable during the contract period does not necessarily have to be limited to the area exclusively allotted to the commercial agent<sup>565</sup>. The fact for a commercial agent to represent an undertaking which competes with his principal without the latter's agreement is serious misconduct that justifies the termination of his mandate<sup>566</sup> without compensation<sup>567</sup>. **The same sanction applies when the competing products marketed were manufactured by the agent and not by a third party<sup>568</sup>.** On the other hand, the search by a commercial agent of substitution activities and the establishment of many contacts with a view to developing an activity intended in the future to compete at least partly and indirectly with his principal, does not constitute serious misconduct but does justify a reduction in the amount of his termination indemnity<sup>569</sup>.

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<sup>564</sup> Commercial Code, Article L. 134-3: "Commercial agents may agree, without needing authorisation, to represent new principals. However, they may not agree to represent an undertaking competing with that of one of their principals without the latter's agreement."

<sup>565</sup> Cass. com., 8 October 2013, LawLex131403.

<sup>566</sup> Cass. com., 11 December 2001, LawLex024864, approving CA Colmar, 1 September 1998, LawLex024701; T. com. Pau, 23 June 1999, LawLex025227: a commercial agent which does not achieve the set targets and represents another brand without the principal's authorization, commits serious misconduct that justifies the termination of the contract without indemnity; CA Paris, 9 October 2001, LawLex024888: the termination by the principal of a commercial agency contract for serious misconduct is justified where the representative concludes a contract that contains similar obligations with a rival.

<sup>567</sup> T. com. Pau, 23 June 1999, LawLex025227: the commercial agent who does not reach the set targets, fails to comply with his duty of information and represents another brand without the principal's authorization commits serious misconduct that justifies the termination of the contract without compensation; Cass. com., 15 February 2000, LawLex025278: representing a competing brand without the express consent of the principal is a serious misconduct of the commercial agent which does not entitle to compensation; Cass. com., 4 July 2000, LawLex025316: a commercial agent's bad performance which is explained by the exercise of a competing activity, constitutes serious misconduct that excludes the benefit of the termination indemnity.

<sup>568</sup> CA Poitiers, 24 April 2018, LawLex18637.

<sup>569</sup> CA Aix-en-Provence, 20 December 2002, LawLex033624.



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However a commercial agent may exercise a representation activity for a company that is not a rival of his principal without committing any fault<sup>570</sup>. The mere representation of another brand does not exclude the right to a termination indemnity where the principal was aware of it<sup>571</sup>. In practice, the representation of a number of principals is very common where the products are not competing and encourages through a synergy effect a boost in turnover, both in the interest of the agent and the various principals. Case law restrictively interprets the concept of competing products. In each case, the court will look at whether even similar products have specific characteristics or whether their use may be specific<sup>572</sup>. **The ranking of the products at issue in the same category as those of the principal by mainstream publications can constitute an indication of their substitutability and therefore of the breach of the legal non-compete obligation**<sup>573</sup>. The commercial agent whose contract provides that the termination indemnity is not due in case of serious misconduct justified by acts of unfair competition, does not breach his non-compete obligation where he represents products that are competing but not substitutable with his principal's products<sup>574</sup>. It has been held that the commercial agent's non-compete obligation not only covers products directly sold by the represented party, but could also cover those it sells under another name or sold by a subsidiary, where these products are identical to those whose distribution is entrusted to the agent<sup>575</sup>.

The non-compete obligation can be set aside. It is thus sufficient for the principal to waive it. In effect, it may be useful in certain business sectors to favor active competition between the products by authorizing the commercial agent to represent several principals. It will then be for the parties to provide for it in a clause of the agency contract.

### IV. Termination of contract

#### A. Termination

##### 4° Serious breach by the agent

#### 7.47. Principle.

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<sup>570</sup> Cass. com., 4 January 2000, LawLex025265, approving CA Lyon, 18 October 1996, LawLex025605.

<sup>571</sup> Cass. com., 25 June 2002, LawLex024206: the fact for the commercial agent of a company that sells traditional kitchens to represent a rival specialized in kitchens sold in large distribution chains, does not constitute misconduct depriving him of termination indemnities and notice where his principal was aware of it; CA Paris, 25 June 1999, LawLex024221: a principal cannot blame its commercial agent for representing a rival where, informed by the agent of the situation when signing the contract, it has itself deleted the non-compete clause initially planned.

<sup>572</sup> See in particular CA Lyon, 8 March 2018, LawLex18419, distinguishing high-end steel framed swimming pools and self-supporting inflatable or tubular pools.

<sup>573</sup> CA Bordeaux, 21 March 2018, LawLex18495.

<sup>574</sup> CA Paris, 8 March 2001, LawLex020659; CA Grenoble, 8 January 1997, LawLex025623.

<sup>575</sup> CA Nancy, 26 November 1997, LawLex025070.



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The cases whereby commercial agency contracts may be terminated without indemnity are restrictively listed by the law. Serious misconduct by the commercial agent therefore deprives him of the compensation set forth in Article L. 134-12 (Commercial Code, Article L. 134-13, 1st indent). The termination cannot be attributed to him for minor misconduct<sup>576</sup>. Serious misconduct is defined as a hardcore breach of a contractual obligation of the contract which makes pursuit of the contract impossible<sup>577</sup>. It may result from a set of breaches by the commercial agent consisting in the disregarding of his contractual undertakings despite reminders from his principal<sup>578</sup>. The Court of Cassation is very demanding in terms of its requirements for a finding of serious breach giving rise to loss of indemnity. Thus, the mere finding that the agent has committed a series of breaches of obligations such as non-compliance with the schedule of visits to customers, failing to provide information to the principal about changes concerning customers, the lack of response to requests for information, non-accountability of its mission and the refusal to participate in business meetings, do not constitute sufficient reasons to deprive the agent of the indemnity, where the courts ruling on the merits did not explain how those breaches also constituted a serious breach<sup>579</sup>.

The court assesses the seriousness of the agent's breach taking account of his independence, since unlike sales representatives (VRP), the agent is not subject to strict orders imposed by the principal. However, as a representative, the agent must comply with his principal's instructions relating to price and commercial policy<sup>580</sup> and with the contractual<sup>581</sup> and legal obligations, such as, in particular, the obligations of loyalty and information.

According to a formula which has now become almost a mantra, a serious breach within the meaning of the case law of the Court of Cassation is "one which infringes the common purpose of the common interest mandate and renders the continuation of the contractual relationship impossible"<sup>582</sup>.

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<sup>576</sup> CA Versailles, 23 March 2000, LawLex025293: a commercial agent must be indemnified when the termination of his contract is based on minor contractual breaches that are not serious misconduct.

<sup>577</sup> CA Reims, 10 September 1997, LawLex025040: Cass. com., 15 October 2002, LawLex02000437: only serious misconduct, i.e. the one undermining the joint purpose of the common interest mandate and making it impossible to continue the contractual link, deprives of the indemnity that compensates for the harm suffered in case of termination of the commercial agency contract.

<sup>578</sup> CA Montpellier, 9 November 1995, LawLex025506.

<sup>579</sup> Cass. com., 21 June 2011, LawLex111156.

<sup>580</sup> CA Paris, 24 September 1997, LawLex025046 which decides that no indemnity is owed to the commercial agent which systematically refuses to submit to the sales methods and is openly hostile with respect to his contracting party.

<sup>581</sup> CA Colmar, 17 November 1992, LawLex025954 retaining that "the refusal to perform his contractual obligations constitutes misconduct by the commercial agent which results in the termination of the contract without termination indemnity".

<sup>582</sup> Cass. com., 15 October 2002, LawLex02000437.



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Accordingly, where the principal tolerates contractual breaches, he is prevented from seeking to rely on them later by claiming a serious breach of contract giving rise to loss of the agent's indemnity<sup>583</sup>.

The difficulties involved in getting out of a contract have resulted in the courts progressively allowing suppliers to stipulate a trial period. The courts of appeal have often been hostile to trial periods on the basis of the mandatory public policy nature of Articles L. 134-12 and L. 134-13 of the Commercial Code, which require the payment of an indemnity on termination of commercial agency agreements, and define those cases in which said indemnity is not payable<sup>584</sup>. The Court of Cassation has on the other hand been favorable to the payment of the indemnity in such cases<sup>585</sup> and has thus accepted durations of six<sup>586</sup> or eight<sup>587</sup> months, holding that an agreement has to be definitively concluded for the status of commercial agent to apply and that this does not prohibit a trial period. This case law appeared to be perfectly justified; if trial periods are accepted under employment law, they would appear to be all the more legitimate for commercial agents, insofar as principals must be able to assess the competence and "fit" of the agent with their commercial policy prior to tying themselves definitively to an extremely rigid contractual relationship. Nevertheless, unsure of the compliance of this solution with Article 17 of Directive No 86/653, the Court of Cassation decided to refer to the Court of Justice<sup>588</sup>. The Court ruled that although the directive neither authorizes nor excludes the stipulation of a trial period, a termination notified during that period cannot deprive the commercial agent of the indemnity<sup>589</sup>. In effect, according to the European Court, the Court of Cassation's postulate, according to which, during the trial period, the contract is not yet definitively concluded, is unfounded. The Court of Justice considers that relations between a commercial agent and a principal subsist as from the time when a contract, the purpose of which is either to negotiate the sale or purchase of goods, or to negotiate and conclude such transactions on behalf of the principal, is executed, irrespective of whether that contract provides for a trial period. Moreover, regardless of when the contract is terminated, the agent is entitled to be indemnified for his past services from which the principal will continue to benefit beyond the termination of the contractual relationship or for the costs and expenses he has incurred in providing those services. The loss of the right to an indemnity enshrined by the French courts would amount to allowing a ground for exclusion not provided for in Article 18 of the directive, whereas that provision, which represents an exception to

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<sup>583</sup> Cass. com., 7 April 2009, LawLex091611; 15 September 2009, LawLex093092; 10 May 2011, LawLex11943.

<sup>584</sup> CA Paris, 6 September 2012, LawLex122152; CA Paris, 30 April 2003.

<sup>585</sup> For before the Decree of 1958 see Cass. soc., 26 November 1959.

<sup>586</sup> Cass. com., 17 July 2001, LawLex024364.

<sup>587</sup> Cass. com., 23 June 2015, LawLex15843.

<sup>588</sup> Cass. com., 6 December 2016, LawLex162033.

<sup>589</sup> CJEU Case C-645/16 Conseils et mise en relations (SARL), Judgment of 19 April 2018, LawLex18760.



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the right to compensation, must be interpreted strictly. Lastly, any interpretation of the directive contrary to the objective of protecting the agent, as in this case, must be excluded. French case law and practice must therefore quickly fall in line with the position of the Court of Justice. The mere stipulation of a trial period will no longer be sufficient to exclude the right to the indemnity. The rigid nature of such a solution will contribute to making commercial agency contracts riskier and less attractive to suppliers.

### **7.55. Legal non-compete obligation.**

Article L. 134-4 of the Commercial Code provides that the agent is governed by an obligation of loyalty with respect to his principal and must perform his mandate in a professional manner. Therefore, he cannot agree to represent an undertaking which competes with its principal's undertaking without the principal's consent<sup>590</sup>. The fact that a commercial agent represents an undertaking that competes with his principal, without the principal's consent, is serious misconduct that justifies the revocation of his mandate without indemnity<sup>591</sup>, even if the contract has not yet been formalized<sup>592</sup>, but does not constitute an act of unfair competition<sup>593</sup>. Likewise, the existence of contractual relationships between the agent and a rival of his principal is serious misconduct which excludes the termination indemnity<sup>594</sup>.

It is not possible for the commercial agent to refuse to distribute the principal's new products on the grounds that the same products are sold through a competing company of which the agent is an active partner<sup>595</sup>. The termination of the agency contract by the principal may also be justified by the agent's poor performance if it is caused by the agent's failure to comply with its non-compete obligation<sup>596</sup>.

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<sup>590</sup> CA Versailles, 9 May 2001, LawLex04248: the commercial agent whose relations with his principal are governed by an obligation of loyalty and a reciprocal duty of information, cannot accept to represent an undertaking which competes with its principal without its knowledge, otherwise he commits serious misconduct depriving him of indemnity.

<sup>591</sup> Cass. com., 11 December 2001, LawLex024864, approving CA Colmar, 1 September 1998, LawLex024701; 15 February 2000, LawLex025278; CA Paris, 9 October 2001, LawLex024888: the termination by the principal of a commercial agent contract for serious misconduct is justified where the representative concludes a contract containing similar obligations with a rival; CA Aix-en-Provence, 3 December 2004, LawLex055668: a commercial agent commits serious misconduct that deprives him of the compensation where he represents the products of a rival in the same sector without the principal's authorization; CA Limoges, 28 October 1996, LawLex025610.

<sup>592</sup> Cass. com., 7 January 2004, LawLex0469: the exclusive commercial agent whose contract is not formalized yet commits a serious misconduct depriving him of indemnities where it accepts to represent an undertaking which competes with that of its principal with the latter's consent.

<sup>593</sup> Cass. com., 7 January 2014, LawLex14490.

<sup>594</sup> Cass. com., 7 October 2008, LawLex081825.

<sup>595</sup> CA Nancy, 26 November 1997, LawLex025070 and CA Grenoble, 8 January 1997, LawLex025623.

<sup>596</sup> Cass. com., 4 July 2000, LawLex025316: a commercial agent's bad performance, which is explained by the exercise of a competing activity, is serious misconduct that excludes the benefit of the termination indemnity; T. com. Pau, 23 June 1999, LawLex025227: the commercial agent who does not achieve the assigned targets fails to comply with its duty of information and represents another brand without the principal authorization commits serious misconduct that justifies the termination of the contract without indemnity.



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On the other hand, the principal who is aware of the dual activity of its intermediary as trader and commercial agent cannot claim the existence of a sale independent to his activity as agent in order to justify a termination of the agency contract for serious misconduct<sup>597</sup>. This is also true where he could not have been unaware of the competing activity going on before signing the agreement and did not object to it<sup>598</sup>. The principal's claim that the agent has breached his non-compete obligation will also not succeed where his other principals offer goods having different features, used for different purposes or which are complementary to the product at issue<sup>599</sup>. **Finally, in a case where the sale of supposedly competing products accounted for only 8% of the agent's turnover, the courts ruled out the existence of a sufficiently serious breach<sup>600</sup>.**

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<sup>597</sup> CA Pau, 15 May 2003, LawLex034474.

<sup>598</sup> CA Aix-en-Provence, 16 March 2011, LawLex11721.

<sup>599</sup> CA Paris, 12 December 2013, LawLex131832; CA Agen, 9 September 2013, LawLex131690, for non-substitutable products.

<sup>600</sup> CA Lyon, 8 March 2018, LawLex18419.



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### V. Consequences of termination

#### A. Compensation of the agent

##### 2° Amount of compensation

#### 7.73. Two-year compensation.

Article L. 134-12 of the Commercial Code provides for the payment of compensation to the commercial agent for the loss suffered because of the termination of the contract by the principal, but does not fix the amount thereof. The customary compensation granted to the commercial agent, to which the contract may refer by reference to usual practices<sup>601</sup>, or where the parties make no express provision<sup>602</sup>, amounts to two years of gross commissions<sup>603</sup> calculated on the basis of the average of the last three years' turnover<sup>604</sup>. The compensation for the termination does not however constitute a lump sum equal to two years of commission but must correspond to the compensation of a loss that the agent can justify having suffered<sup>605</sup>. In effect, no law or regulation imposes the payment of two years of commissions as compensation for the termination of a commercial agency contract<sup>606</sup>. Some trial courts consider that the two-year compensation is not automatically owed to the agent who must justify a corresponding loss<sup>607</sup>, in particular where the duration of the contract has been less than two years<sup>608</sup>. Other courts, on the contrary, consider that in the absence of any proof of a smaller loss, the compensation paid to the agent in accordance with usual practices must be two years of remuneration<sup>609</sup>, or that the compensation must be equal to two years of commissions regardless of the amount of the loss claimed by the agent<sup>610</sup>. The amount of the compensation cannot however exceed the two-year compensation on the grounds

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<sup>601</sup> CA Nancy, 17 September 1997, LawLex025045: customs of the profession, to which the contract refers, generally fix the amount of the compensation for termination at two years of commissions.

<sup>602</sup> CA Bordeaux, 3 December 1997, LawLex024983.

<sup>603</sup> Cass. com., 28 May 2002, LawLex024168. See also, for example, CA Pau, 14 December 2009, LawLex10213; CA Reims, 6 September 2004, LawLex055664; CA Bordeaux, 22 April 1997, LawLex025659.

<sup>604</sup> T. com. Paris, 7 January 2003, LawLex042184.

<sup>605</sup> CA Nîmes, 3 April 2003, LawLex034438.

<sup>606</sup> CA Paris, 20 January 1995, LawLex025437; 25 February 2004, LawLex041603.

<sup>607</sup> CA Colmar, 26 January 2012, LawLex12261 : le juge ne peut se contenter de se référer aux usages pour déterminer le montant de l'indemnité de rupture due à l'agent commercial, sans apprécier, eu égard aux circonstances de la cause, l'étendue du préjudice effectivement subi.

<sup>608</sup> CA Toulouse, 11 January 2005, LawLex054615; CA Nîmes, 3 April 2003, LawLex034438: The compensation for termination does not constitute a lump sum equivalent to two years of salary but must correspond to the compensation of a damage that the agent justifies having suffered; CA Paris, 3 April 2014, LawLex141832, refusing the payment of the indemnity on the ground that the relationship only lasted 29 months; CA Caen, 19 November 2015, LawLex20151697: one year and a modest contribution of customers do not justify an indemnity of 2 years' commission; CA Rennes, 3 May 2016, LawLex16911.

<sup>609</sup> CA Caen, 25 October 2007, LawLex081939; CA Nancy, 23 March 2016, LawLex16702, In this case, the agent had only worked for thirteen months for the account of the principal, but had been selling the brand in question for several years when it was taken on by the principal and the latter was unable to show that the harm resulting from the termination amounted to less than two years of commission.

<sup>610</sup> T. com. Paris, 9 December 2003, LawLex042170.



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that the termination of the mandate occurred at the time the agent was negotiating the transfer of his clientele to a third party and that because of it he had lost that opportunity<sup>611</sup>.

According to the Court of Cassation<sup>612</sup>, determining the amount of the compensation for termination falls within the discretion of the trial courts. The indemnity should therefore not systematically and automatically be two years of commissions<sup>613</sup>. The courts generally take into consideration the duration of the mandate, or the decrease in the turnover suffered by the agent due to the termination<sup>614</sup>. In practice, the amount of the compensation for termination paid by the principal to his agent often amounts to two years of gross commissions<sup>615</sup>, especially where their cooperation has been productive and loyal for long periods, such as three and a half<sup>616</sup>, seven<sup>617</sup>, eleven<sup>618</sup>, sixteen<sup>619</sup> or thirty<sup>620</sup> years. The sudden nature of the termination can also justify the payment of two years' commission. This is the case where the agency agreements is terminated early for serious breaches that have not been established<sup>621</sup>. On the other hand, the short duration of the contractual relationships may deprive the commercial agent of the customary compensation<sup>622</sup> or give rise to an indemnity of less than the two-year compensation<sup>623</sup>. The small increase in the agent's turnover and the short duration of the activity<sup>624</sup> or the small amount of the investments made<sup>625</sup> may justify, in particular, the payment of one year of

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<sup>611</sup> CA Rouen, 6 December 2012, LawLex122468.

<sup>612</sup> Cass. com., 14 June 2005, LawLex056644.

<sup>613</sup> CA Versailles, 27 October 2005, LawLex06758; CA Grenoble, 25 June 2008, LawLex092836: the commercial agent whose fixed-term contract is not renewed is not automatically entitled to the two-year indemnity but only to an indemnity intended to compensate his actual loss.

<sup>614</sup> Cass. com., 22 September 1999, LawLex02000436, approving CA Lyon, 26 March 1999, LawLex03664; CA Paris, 20 October 2004, 3 judgments, LawLex043390, LawLex043391, LawLex043393: given the length of the parties' relationships, the virtually exclusive nature of the agent's activity and the existence of a non-compete clause, the compensation for termination must be two years of commissions.

<sup>615</sup> See, for example, CA Pau, 22 May 2006, LawLex061837; CA Besançon, 30 September 2009, LawLex10203; CA Versailles, 7 January 2010, LawLex10393.

<sup>616</sup> CA Angers, 21 June 2005, LawLex06343.

<sup>617</sup> CA Paris, 25 February 2004, LawLex041603.

<sup>618</sup> CA Besançon, 10 September 1997, LawLex024989.

<sup>619</sup> CA Paris, 29 March 2018, LawLex18545.

<sup>620</sup> CA Versailles, 22 November 2012, LawLex122393.

<sup>621</sup> CA Agen, 12 June 2013, LawLex131015, ordering the principal to pay to the agent, in addition to the two-year compensation, an indemnity covering the loss of commissions up to the end of the contract and damages for sudden and vexatious termination.

<sup>622</sup> CA Paris, 13 February 1991, LawLex025825; CA Aix-en-Provence, 4 February 1997, LawLex025637: the compensation for termination that is customary in the area of the commercial agency does not benefit the agent who has only been active for a few months; 27 February 1997, LawLex025646: the agent who has exercised his duties only for seven months cannot claim a compensation for termination amounting to two years of commissions; CA Lyon, 29 April 1999, LawLex025205: the compensation for termination cannot amount to two years of commissions where the contract has only been subject to a short-term performance. But see CA Pau, 14 December 2009, LawLex10213: in accordance with practice, the commercial agent is entitled to compensation for termination determined on the basis of two years of commissions, regardless of the length of the contractual relationship.

<sup>623</sup> CA Versailles, 6 December 2012, LawLex122467, stressing that the loss actually suffered by the agent may be lower because of the brevity of the duration of the contractual relationship due to the fact that he is a multi-brand representative and that has not shown proof of having made investments specific to the performance of the contract.

<sup>624</sup> CA Rouen, 18 October 1990, LawLex024986.

<sup>625</sup> CA Besançon, 18 May 2011, LawLex111056.



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commissions instead of the customary two years. The same would appear to apply where the agent has not made it possible to build any real customer base but has benefitted from the network belonging to its principal<sup>626</sup>. Where the two-year compensation is granted for short periods of cooperation, it seems that the circumstances of the termination, i.e. sudden and without notice, have been the reason behind such remedy<sup>627</sup>.

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<sup>626</sup> CA Paris, 24 May 2018, LawLex18784.

<sup>627</sup> Cass. com., 14 May 2002, LawLex024162, upholding CA Paris, 24 September 1999, LawLex024167: a commercial agent who has only been active for 7 months and whose contract has been terminated suddenly and without notice is entitled to the customary two-year compensation, irrespective of whether, after temporarily being an employee, he could re-establish himself, without the non-compete clause in the contract being relied upon against him; CA Nancy, 22 September 1999, LawLex025237: the sudden termination of the commercial agent's open-ended contract entitles him to compensation which may be equal to two years of gross commissions.