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Breach of business relationships in an international context: how to determine the applicable law?

In a decision dated March 25, 2014, the Commercial Chamber of the *Cour de Cassation* (French Supreme Court) ruled on the sensitive issue of the determination of the law applicable in case of breach of business relationships[1].

Under French law, Article L. 442-6, I, 5° of the French Commercial Code (the "FCC"), which provides for the payment of an indemnification in case of sudden breach of established business relationships, is a significant source of commercial litigation[2].

Its implementation in an international context, i.e. when one of the contractual parties is not French, often creates conflicts of laws and jurisdictions that can be summarized as follows: when can this legal provision be invoked and who is the competent judge?

In the commented case, a Chilean company had been distributing the luxury perfumes and cosmetics of a French group on the Chilean territory since 1991. In 1999, the two parties entered into a three-year renewable distribution contract. In 2003, the French group terminated the contract, with immediate effect.

The Chilean company brought the matter before the French judge and sought compensation for the loss it alleged to have suffered as a result of the sudden breach of the business relationships.

The Paris Commercial Court and, then, the Paris Court of Appeals, held that French law was applicable. This analysis was subsequently confirmed by the *Cour de Cassation* that specified as follows:

"The law applicable to extra-contractual liability is that of the State of the place where the harmful event occurred and that place refers to both the place where the event giving rise to the damage occurred and the

place where that damage itself occurred; (…) in case of a legal situation extending over different locations, it is necessary to determine the State which is most closely connected with the harmful event".

As private international law typically makes a distinction between contractual matters and tort matters, the question of the characterization of liability in relation to a claim brought on the basis of Article 442-6, I, 5 of the FCC quickly arose.

The *Cour de Cassation* has settled this issue for some years now: it is now established that a party who terminates an established business relationship is liable in tort under Article L. 442-6, I, 5° of the FCC[3].

As the terminating party was liable in tort, French courts found that the law applicable to the dispute was that of the State of the place where the harmful event had occurred. This is a French conflict of law rule established in the so-called *Lautour* decision issued by the *Cour de Cassation* and consistently applied and extended to all civil-liability matters since then.

This solution could not indeed be inferred from European conflict of laws rules: The Rome Convention of June 19, 1980 only deals with the law applicable to contractual obligations and Regulation (EC) 864/2007 of July 11, 2007 on the law applicable to non-contractual obligations, commonly referred to as the Rome II Regulation, does not apply to events giving rise to damage that occurred prior to August 20, 2007 (this Regulation applies the following principle: *"the law applicable to a non-contractual obligation arising out of a tort/delict shall be the law of the country in which the damage occurs irrespective of the country in which the event giving rise to the damage occurred"*).

In 2008, in a similar case, the *Cour de Cassation* had already ruled that "*the law applicable to this liability is that of the State of the place where the harmful event occurred*" but incomprehensibly based its decision on Article 5 of Council Regulation (EC) No 44/2001 of December 22, 2000 on jurisdiction[4] (this Article stipulates that in matters relating to tort, delict or quasi-delict, the competent court is that of the place where the harmful event occurred or may occur).

However, the applied French conflict of laws rule contains an ambiguity: the harmful event has two components, i.e. "*the event giving rise to the damage*" and "*the place where the damage occurred*".

When these two elements are located in the same country, there is no difficulty in determining the applicable law. Yet, when these two elements are located in different countries (in the commented decision, the Paris Court of Appeals held that the event giving rise to the damage was the breach of the contract in France by the French Company) or if there are several events giving rise to a damage and /or several damages, the issue becomes a legal situation extending over different locations and several laws may be deemed applicable.

In that case, the applicable law ought to be determined under the so-called "principle of proper law" by which judges are supposed to identify on a case-by-case basis the "*country that is the most closely connected with the harmful event*".

This rule has been consistently applied by French courts since the *Gordon and Breach* decision rendered by the *Cour de Cassation* in 1997.

In the commented case, France was the State the most closely connected with the harmful event. According to the *Cour de Cassation*, this close connection resulted *"from the pre-existing 12-year contractual relationships between the parties that the latter formalized through the conclusion of contract in Paris that designated French law as the applicable law and the Paris Commercial Court as the competent jurisdiction*".

The French terminating party had argued that the applicable law was that of the State where the harmful event occurred – without any distinction between the two elements of this harmful event – and claimed that Chili was that State.

However, it failed to convince the French judges who usually favor an extensive application of Article L. 442-6, I, 5° of the FCC.

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[1] Commercial Chamber of the *Cour de Cassation*, March 25, 2014, n°12-29534.

[2] Article L. 442-6, I, 5° of the French Commercial Code: *"The following acts committed by any producer, trader, manufacturer or person listed in the trade director shall trigger the liability of their perpetrator and obligate said perpetrator to compensate the harm caused thereby:*
5° (...) suddenly terminating, even partially, an established commercial relationship without prior written notice commensurate with the duration of the business relationship and consistent with the minimum notice period determined by the multi-sector agreements in line with standard commercial practices (...). The preceding provisions do not affect the ability to terminate the relationship without prior notice if the other party has failed to comply with its obligations or in cases of force majeure."

[3] Commercial Chamber of the *Cour de Cassation*, February 6, 2007, n°04-13.178; October 21, 2008, n° 07-12.336; January 13, 2009, n° 08-13.971; September 15, 2009, n° 07-10.493; May 11, 2010 n° 09-10.797; January 18, 2011, n° 10-11.885; December 13, 2011, n° 11-12.024.

[4] Commercial Chamber of the *Cour de Cassation*, October 21, 2008, n° 07-12336.

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