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New illustration of a breach of an established business relationship in the context of an international dispute

French legal provisions applicable to sudden breaches of established business relationships are frequently applied in the framework of cross-border disputes between French and foreign companies, irrespective of which company is the terminated or the terminating party.

By a decision rendered on May 20, 2014 in relation to a dispute between French companies and their Dutch clients, the Commercial Chamber of the *Cour de Cassation* (French Supreme Court) provided a new illustration of how the provisions set forth in Article L. 442-6 I §5 of the French Commercial Code were to be applied in an international context.

This decision was also an opportunity for the *Cour de Cassation* to rule on two ancillary issues: the wrongful interference of the Dutch parent company and the joint and several liability of the latter with its subsidiaries that terminated the established business relationship.

The sudden breach of an established business relationship is one of the most frequent causes of action in business litigation matters in France. "Sudden breach" means that the termination was not preceded by a written notification providing for a sufficient notice period given the applicable commercial practices and multi-sector agreements, the circumstances surrounding the business relationship and the length of such relationship. The sudden breach of an established business relationship is sanctioned – as everyone now knows – by Article L. 442-6 I §5 of the French Commercial Code (the "FCC").

The application of French rules governing the sudden breach of an established business relationship is not limited to business relationships between French companies. These rules – that are considered as overriding mandatory provisions – can also be applied to international disputes, irrespective of whether the terminated party is a French company or a foreign company.

In international disputes, it is, however, necessary to preliminarily determine the law that governs the

business relationship at stake, by using national, EU or international conflict-of-law rules.

The determination of the applicable law is, therefore, a critical issue.

In the commented decision[1], the *Cour de Cassation* (French Supreme Court) applied French rules to an intra-EU dispute concerning the breach of an established business relationship.

This dispute was between a French company specialized in the manufacture of technical yarns that, directly or through its French subsidiary, had business dealings with two companies belonging to a Dutch group.

After more than 20 years of business relationships, the companies entered in June and July 2006 into two long-term supply agreements with a three-year duration each and an expiry date set on December 31, 2008. One of these agreements also included an automatic renewal clause that could be waived subject to a written notification by registered letter, return receipt requested, at least two months before the contractual expiry date.

The group strategy for the two Dutch companies was to implement a vertically integrated production process. The first company terminated its supply agreement beyond the contractually required two-month notice period, and the second company notified by an email dated December 2008 that it would cease placing orders in 2009.

The two French suppliers decided to bring a liability action against the first one for faulty termination as a result of an abuse of dominant position and abuse of economic dependence, and against the second one for sudden breach of an established business relationship within the meaning of Article L. 442-6 I §5 of the FCC.

The two French companies also claimed that the parent company of the Dutch Group had interfered in the business relationships of its subsidiaries and requested that it be ordered, jointly and severally with the subsidiaries, to provide compensation for the loss suffered.

As such, French judges had to rule on *(I)* the applicability of French law applicable to sudden breaches of established business relationships, *(II)* the wrongful interference of the parent company of the two companies that had terminated the business relationship, and *(III)* the existence of an abuse of dominant position and abuse of economic dependence. Only issues *(I)* and *(II)* related to the sudden breach of the business relationship are addressed in this article.

I. The application of Article L. 442-6 I §5 of the FCC in the context of an international dispute

1 – The first question that judges had to answer was whether French provisions related to sudden breaches of established business relationships were applicable and enabled the French suppliers to claim that their Dutch clients were to be held liable in tort[2].

2 – Quite recently, the *Cour de Cassation* ruled on the determination of the law applicable to an international dispute related to a breach of an established business relationship between a Chilean distributor and a French supplier[3].

In that particular case, the Chilean distributor was the terminated party and sought the application of Article L. 442-6 I §5e of the FCC to the detriment of its French supplier.

When adjudicating this case, the *Cour de Cassation* applied the French conflict-of-law rules and held that France was the State most closely connected with the harmful event as *(i)* the contract had been signed in Paris, *(ii)* specified that the governing law was French law, and *(iii)* stipulated that the competent court was the Commercial Court of Paris. It inferred therefrom that the place where the damage occurred was France and that the provisions set forth in Article L. 442-6 I §5 were, therefore, duly applicable.

3 – In the commented decision, the French companies, i.e. the terminated parties, sought the application of Article L. 442-6 I §5 of the FCC to the detriment of their Dutch clients.

On the other hand, the Dutch companies contented that the form of a contract was governed by the law of the State were such contract was performed and that the formal conditions surrounding the termination of an established business relationship were governed by the law of the State where that contract was terminated.

They argued that the gradual termination of the business relationships had been notified to the French suppliers during a meeting held in September 2005 in the Netherlands, which the French suppliers had acknowledged in an email dated October 2005.

As such, they claimed that the termination was absolutely lawful under Dutch law that was alternatively applicable pursuant to the Rome II Regulation II[4].

This Regulation sets forth that *"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 and irrespective of the country or countries in which the indirect consequences of that event occur."*, or the law of the country with which *"the tort/delict is manifestly more closely connected"*[5].

The *Cour de Cassation* upheld the judgment of the Court of Appeals[6] that had pointed out that the damage was the result of the suddenness of the termination, not of the termination itself.

It held that **the place of the relevant damage was France, i.e. the place where the terminated parties conducted their business operations**.

As such, it did not take into account the fact that the notification of the gradual termination of the business relationship had been made in the Netherlands, as this element was not relevant in establishing that this

country would be most closely connected with the harmful event and that Dutch law would be the applicable law.

The *Cour de Cassation* thus ruled that **the provisions set forth in Article L. 442-6 I §5 of the FCC were applicable to the dispute**.

4 – After having determined the applicable law, the *Cour de Cassation* also examined the question of whether the business relationship was "established", within the meaning of French law, a fact which was disputed by the two Dutch companies.

Indeed, Article L. 442-6 I §5 of the FCC applies where the business relationship between the parties prior to termination was **ongoing, stable and regular**, and where the terminated party could reasonably anticipate for the future a continued business flow with its trading partner[7].

When the business relationship is an established relationship, the terminating party must send a **written and unambiguous termination notice** that must provide for a **sufficient notice period** and **clearly, firmly and definitely express its intention to terminate the business relationship**, in order to make sure that the termination will not be sudden[8].

In addition, French courts consider that the terminating party is at fault if it has given its partner the legitimate hope of a continuation of the business relationship[9].

In the commented decision, the *Cour de Cassation* upheld the judgment of the appellate judges who, after having acknowledged that *(i)* the parties had, until 2009, discussed the purchase volume and pricing, as well as the continuation of the business relationship up to 2010, and *(ii)* the volume of orders had increased between 2006 and 2008, considered that the Dutch companies had not shown a firm and definitive intent to terminate the business relationship.

In these circumstances, the French suppliers had, according to the appellate judges, reason to believe that the business relationship, the established nature of which were to be considered as maintained, was sustainable and would continue.

Consequently, the *Cour de Cassation* held that, given the circumstances of the case (i.e. the length, the breadth, and the evolution of the business relationship, the fact that such relationship was established, the specificity of the manufactured and marketed products, market difficulties, the Dutch companies' will to "verticalize" their business and thereby compete with their French suppliers), **a notice period of one year** should have been applied by the Dutch companies.

II – The parent company's wrongful interference in the termination of the business

relationship by its subsidiaries

1 – Another interesting aspect of the commented decision was the issue of determining whether the Dutch parent company could be considered as co-terminating party and, as such, be held jointly and severally liable with its subsidiaries in this respect.

Indeed, the two French suppliers had requested the court to hold the Dutch parent company jointly and several liable for wrongful interference in the performance and termination of the two supply agreements.

They contended that the parent company, by instructing its subsidiaries to suddenly terminate the business relationship in breach of their legal or contractual obligations, had committed a fault that made it personally liable.

2 – Under applicable case-law, a parent company can, as co-terminating party of a business relationship, be held jointly and severally liability with its subsidiaries but only in a limited number of cases.

For the parent company to be considered as co-terminating party and, as such, be held jointly and severally liable with its subsidiaries, French judges demand proof that the parent company had **directly and actively** interfered in the business relationship of its subsidiaries or in the termination of the same[10].

The assessment of the parent company's active interference is made on a case-by-case basis.

The commented decision provides a further illustration of how judges assess this situation.

3 – In the matter at hand, the French companies contended that the Dutch parent company had imposed on its subsidiaries, as part of a premeditated group strategy, the obligation to discontinue the business relationship.

The appellate proceedings had indeed established that the two Dutch subsidiaries had followed the instructions and the strategy of their parent company when they discontinued the business relationship with their French suppliers.

4 – Yet, the appellate judges had also acknowledged that the officers of the two Dutch subsidiaries, in their capacity as representatives of these companies, had been involved in the discussions, negotiations and relationships with the French companies, contrary to the parent company that was not represented in this respect.

The appellate judges had held that there was no evidence of an active interference that would establish that the parent company had been **personally** involved in the performance of the agreements and in the conditions in which such agreements had been terminated. In particular, no consequences could be drawn from the simultaneousness of the terminations insofar as the termination dates corresponded to a contractual expiry date agreed upon by the contracting parties.

Lastly, the Court of Appeals had noted that the Dutch subsidiaries were **not deprived of legal and business**

autonomy, that they had their own corporate officers who negotiated and proposed contractual addenda, in particular regarding pricing, and that it was these officers who expressed their intention not to continue the business relationship.

5 – Consequently, the Court of Appeals had ruled that the parent company, that had **not committed any civil wrongdoing** as it did not interfere in the management of its subsidiaries to such an extent that the latter **would have completely lost their autonomy and legal personality**, could not be held liable.

The *Cour de Cassation* logically upheld the part of the appellate judgment addressing this point.

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[1] Commercial Chamber of the *Cour de Cassation*, May 20, 2014, n°12-26705

[2] According to an established case-law of the Commercial chamber of the *Cour de Cassation*, a claim concerning the sudden termination of an established business relationship brought under Article L. 442-6 I §5 of the FCC is a tort action and the terminating party is, therefore, liable in tort, not contractually (cf. for instance, Commercial chamber of the *Cour de Cassation*, December 13, 2011, n°11-12024).

[3] Commercial chamber of the *Cour de Cassation*, March 25, 2014, n°12-29534 – cf Soulier April 2014 e-newsletter.

[4] Regulation (EC) No 864/2007 of the European Parliament and of the Council of July 11, 2007 on the law applicable to non-contractual obligations (Rome II), applicable to events giving rise to damage that occur after August 20, 2007.

[5] Article 4 of the Rome II Regulation.

[6] Court of Appeals of Lyon, September 6, 2012, n°10/05522.

[7] 2008 Annual report of the *Cour de Cassation*, http://www.courdecassation.fr/IMG/pdf/Cassation_2008.pdf, p. 307; Commercial Chamber of the *Cour de Cassation*, May 5, 2009, n° **08-11916.**

[8] Commercial Chamber of the *Cour de Cassation*, November 20, 2012, n°11-22660.

[9] Court of Appeals of Paris, February 3, 2011, n°08/18087.

[10] Cf. for instance Commercial Chamber of the *Cour de Cassation*, September 11, 2012, n°11-17458

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