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The freedom to negotiate prices: A significant imbalance is where the courts draw the line

In a ruling of 25 January 2017 (case no. 15-23.547), France's highest civil court, the Cour de Cassation, substantially extended the scope of article L442-6 I 2° of the French Commercial Code, which prohibits a party from imposing obligations on their business partner that would result in a significant imbalance, by holding that that article allows *"the court to check the price insofar as it was not freely negotiated and creates a significant imbalance between the rights and obligations of the parties"*. This is in several ways a remarkable ruling.

The context

The case was about a claim issued against Galec (the Leclerc group's purchasing organization) by the French Finance Minister concerning 118 contracts with 46 suppliers (the so-called "single annual agreements" summarizing the general terms of the parties' business relationship that they must basically renegotiate each year). Galec was ordered to refund 61.3 million euros to the suppliers and to pay a 2 million euro civil fine.

The court's analysis of Galec's practices

On 01 July 2015 (see our newsletter of October 2015), the Paris Court of Appeal had found that two of the contracts' clauses amounted to restrictive business practices in the meaning of article L442-6 I 2°:

- the payment of an **end-of-year rebate to Galec for an unknown or ridiculously low consideration** (i.e., an indeterminate amount of turnover or barely half the turnover achieved the previous year) and
- a **monthly advance payment on the end-of-year rebate to be effected before Galec paid for the delivered goods**.

The Cour de Cassation upheld the Paris Court of Appeal's (rather traditional) two-step approach, finding first that there was indeed a significant imbalance between the rights and obligations of the parties – here due to the lack of any consideration – and then ruling that Galec had imposed such a significant imbalance on its suppliers on the grounds that the disputed clauses had not been negotiated at all.

The principle established by the court

From a legal standpoint, the Cour de Cassation's decision is remarkable because it means that the courts may in a way check the purchase price (specifically, the result of the business negotiations concerning the quid pro quo for the discounts or rebates granted by the seller to the buyer). Such a ruling was far from self-evident, because firstly, price checks are excluded from the scope of article 1171 indent 2 of the French Civil Code (as amended by the ministerial order of 10 February 2016) and article L212-1 of the French Consumer Code, which both prohibit significant imbalances in contracts; secondly, article L442-6 I 2° of the French Commercial Code literally only applies to "obligations", not the specific amount which the seller undertakes to pay; and thirdly, price checks by the courts might contravene the principle enshrined in the French Commercial Code, that the parties may freely negotiate pricing terms.

However, the Paris Court of Appeal, and the Cour de Cassation after it, found that article L442-6 I 2° of the French Commercial Code followed its own logic (especially where mass retailers are concerned...) independently of the French Civil Code's or Consumer Code's goals and that price checks did not jeopardize the principle of the free negotiation of pricing terms insofar as they were circumscribed to identifying significant imbalances resulting precisely from a lack of negotiations.

France's highest civil court therefore affirmed *"that the principle according to which the parties may freely negotiate [pricing terms] is not limitless and that the lack of any consideration or justification for the contracting parties' obligations, even where such obligations do not fall into the business cooperation services category, may be prohibited by article L442-6 I 2° of the French Commercial Code where a business partner imposes them or attempts to impose them and they create a significant imbalance"*.

The effective reach of the court's decision

✓ A comprehensive and consistent system of checks?

First of all, the Cour de Cassation adds to the system of checks that applies to contractual rights and obligations: Article L442-6 I 1° prohibits business partners from obtaining any benefit whatsoever that is not compensated by an effective commercial service or that is evidently disproportionate in regard of the service's value, whereas article L442-6 I 2° prohibits the lack of effective consideration for price reductions awarded to the buyer by the seller. This broad view of the **judicial checks** to which are subject **the business cooperation's financial terms on the one hand** (article L442-6 I 1° of the French Commercial Code) **and the purchase price on the other hand** (article L442-6 2° of the French Commercial Code) is all the more crucial as operators can be taken to court not only by their business partners but also by the president of the French competition agency, Autorité de la Concurrence, French public prosecutors, and the French Finance Minister.

✓ End-of-year rebates are not systematically invalid

The decision's reach is **limited to practices that are actually unlawful**. An end-of-year rebate does not necessarily create a significant imbalance: it is the lack of any effective consideration for the rebate that is prohibited (in the case at hand, the court found that the consideration was either indeterminate or ridiculously low). Likewise, advance payments on end-of-year rebates are not unlawful in and of themselves, but here the court found them to be so after comparing them to the payment terms for the purchased goods (payment of the price after advance payment on the rebate, thereby generating unwarranted cash for Galec).

✓ Too formal a check?

Lastly, the reach of the decision is subject to the second requirement of article L442-6 I 2°: **proof that the operator imposed or attempted to impose the obligation creating the significant imbalance**. In the case at hand, the Cour de Cassation confirmed the Paris Court of Appeal's finding that the disputed clauses had been imposed by Galec on the grounds that they were drawn up in advance and *"formed a non-negotiable component of all reviewed contracts"*. Furthermore, the Court of Appeal noted that even though the end-of-year rebate rate varied between suppliers, the simple fact that they had all initialled and signed the master agreements and their appendices without any reservations or corrections in that regard was proof that there had not been any effective negotiations and that the clauses had been imposed. The disputed clauses (end-of-year rebate without any effective quid pro quo, out-of-balance mutual financial undertakings) would may be not have been found to be unlawful if it could have been proven that the parties did in fact negotiate terms and that the price reduction was freely granted in the course of the negotiations.

Conclusion

Operators using **boilerplate (master) agreements liable to be signed as is** (financial or commercial lessors, franchisors, licensors, etc.) must be careful as to how they draw up their contractual documentation and how they negotiate not only commercial but also financial terms in order to avoid being sued for imposing a significant imbalance.

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