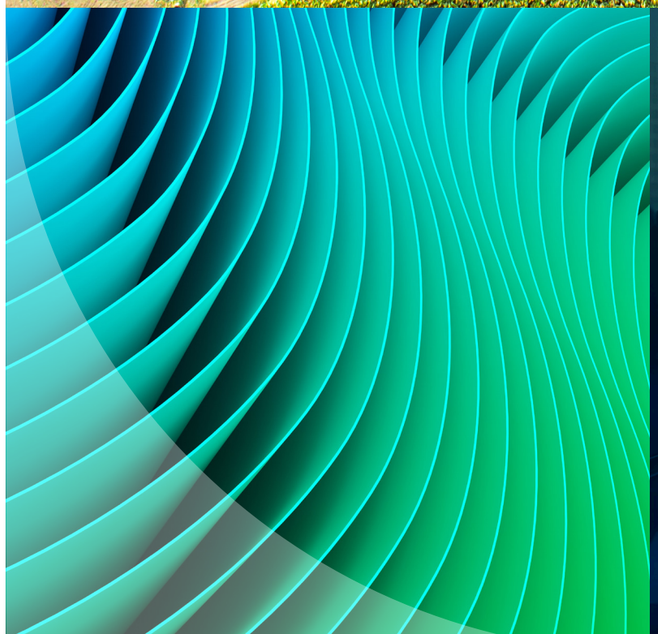
Linklaters

Addressing contractual imbalances in the agricultural and food sectors

New legislative insights



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Introduction

In the spring of 2024, in response to growing concerns within the agricultural and food sectors, the Belgian executive power made an in-depth examination of the supply chain dynamics. Its investigation revealed that multiple actors along the supply chain – suppliers, farmers, and franchisees – are often at a disadvantage, facing contractual imbalances imposed by economically stronger entities, typically supermarket chains, acting as buyers or franchisors.

This context led to the adoption of two Royal Decrees in early summer 2024:

A

The Royal Decree on relationships within the agricultural and food supply chain ("Royal Decree of 4 July 2024"):

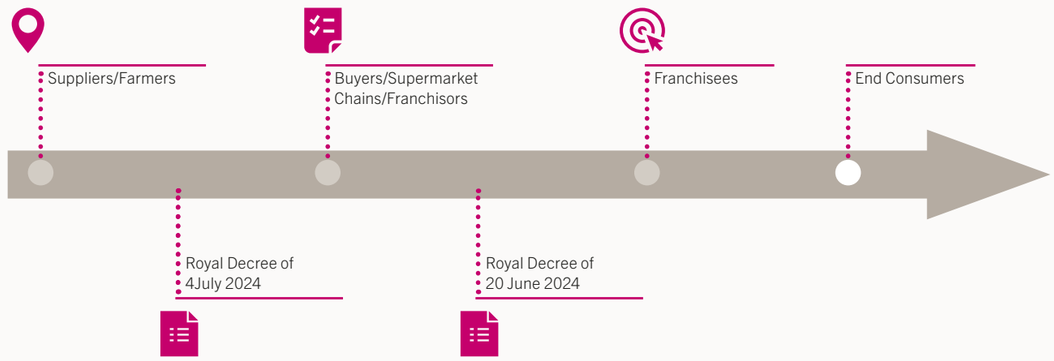
this Decree supplements the existing lists of unfair trading practices in business-to-business relationships within the agricultural and food supply chain.

B

The Royal Decree on partnership agreements ("Royal Decree of 20 June 2024"):

this Decree supplements the existing list of unfair terms for commercial partnership agreements concerning retail trade in non-specialised stores with a predominance in food.

For the purpose of our analysis, we define the supply chain as follows:



In this newsletter, we delve deeper into the implications of these legislative changes and how they aim to rectify the power imbalances in the agricultural and food supply chain. We will first analyse the context surrounding the adoption of these Royal Decrees (**Section 2**) and their scopes of application (**Section 3**). The newsletter then details the new blacklisted trading practices and clauses (**Section 4**) and greylisted trading practices and clauses (**Section 5**), concluding on the application in time of the Royal Decrees (**Section 6**).

2 Contextualisation

The Royal Decree of 4 July 2024

The Act of 28 November 2021 transposes Directive 2019/633 on unfair trading practices in business-to-business relationships in the agricultural and food supply chain ("**UTP Directive**"), leading to the adoption of Articles VI.109/4 to VI.109/8 of the Code of Economic Law ("**CEL**") (see our previous newsletter on this topic).

Despite the transposition of the Directive, it seems that the situation of the weaker parties in the agricultural and food supply chain (i.e. the suppliers) has not improved.

The adoption of the Royal Decree of 4 July 2024 follows **multiple crises and strikes from the agricultural world in 2024**, highlighting the extremely challenging conditions in which these professionals operate, as well as potential **abuses by their stronger contractual counterparts**. Their preoccupations pertain to price volatility, very weak profits (or even, losses), and often non-transparent and imbalanced contractual relationships with their buyers.

Discussions held with various stakeholders of the agricultural world have underscored the need to adopt a stronger legal framework to address these issues. Key points include prohibiting buyers from purchasing products at a price lower than the suppliers' production costs, banning unfair delisting of products, prohibiting refusal to renegotiate contracts in the event of unforeseeable circumstances, and prohibiting trading practices deemed unfair (e.g. imposition of excessive or unjustified penalties or automatic unilateral set-off).

It is on this basis that the Royal Decree of 4 July 2024 introduces **additional blacklisted and greylisted trading practices to those already enumerated in Articles VI.109/5 and VI.109/6 of the CEL**.

The Royal Decree of 20 June 2024

The Royal Decree of 20 June 2024 **adds clauses to the lists of blacklisted and greylisted B2B unfair terms** included in Articles VI.91/4 and VI.91/5 of the CEL. This Decree specifically **applies to commercial partnership agreements concerning retail trade in non-specialised stores with a predominance in food**. In other words, it targets franchise contracts concluded between supermarket chains and independent grocery stores.

The adoption of this Decree was justified by several factors, among which the fact that the food distribution sector in Belgium is characterised by the presence of a small number of operators (franchisors) who generally hold a strong position in their relationships with their commercial partners (franchisees), especially when it comes to SMEs. Independent operators such as franchisees are, in practice, often subjected to a very significant degree of legal and economic dependency. This economic dependence is reflected in the fact that the negotiating leverage of these franchisees is very limited and sometimes non-existent. For example, during negotiations for the potential renewal of their contracts, franchisees often find themselves forced to accept new conditions imposed by their contracting parties in order to continue operating the business in which they have made significant investments.

These statements prompted the Belgian executive power to analyse several contracts concluded between supermarket chains and independent grocery stores, highlighting the necessity of prohibiting certain terms deemed to cause excessive harm to the weaker party in the contract.

The scope of protection of the Royal Decree of 20 June 2024 is quite different from that under the original B2B Act[1]: Article VI.91/3 of the CEL specifies that the assessment of the abusive nature of contractual terms does not target the core obligations of the parties. However, when analysing the Royal Decree of 20 June 2024, we observe a shift in the scope of protection of the weaker parties to contracts, as the protection now provided by the latter **covers non-core and core obligations of the franchisees and the franchisors**.

[1] Act of 4 April 2019 amending the Code of Economic Law in relation to abuses of economic dependence, unfair terms and unfair trading practices between undertakings, B.S., 24 May 2019.

3 Scopes of application

The Royal Decree of 4 July 2024

The scope of application of the Royal Decree of 4 July 2024 does not differ from that of Article VI.109/4 of the CEL: it applies to the sale of agricultural or food products by suppliers whose turnover does not exceed EUR 350,000,000 (except for certain recognised supplier organisations, for which there are no limits on their turnovers). The legislator considers these suppliers as vulnerable, regardless of the turnover of their buyers, which means that the Act will always apply to them.

In the preparatory works of this Royal Decree, the Belgian executive power reiterates several times that, as with Articles VI.109/4 to VI.109/8 of the CEL, **it does not only target abusive contractual clauses, but also abusive trading practices. This includes not just clauses, but also every act, omission or behaviour.**

The Royal Decree of 20 June 2024

The Royal Decree of 20 June 2024 is applicable to commercial partnership agreements as defined in Article I.11, 2° of the CEL, meaning "*agreement[s] concluded between several persons, whereby one of these persons grants the other the right to use, for the sale of products or the provision of services, a commercial formula in one or more of the following forms: (i) a common sign; (ii) a common trade name; (iii) a transfer of know-how; (iv) commercial or technical assistance*". This typically refers to but is not limited to franchise contracts. As for the definition of "*retail trade in non-specialised stores with a predominance in food*", this Royal Decree refers to the **NACE code 47.11**.

These new rules do not prejudice the rules relating to **pre-contractual information obligations** listed in Articles X.26 and following of the CEL. There is also no redundancy, as Articles X.26 and following of the CEL aim solely at the pre-contractual information of the franchisee, whereas the Royal Decree aims at the **effective and substantive protection of the latter during the actual performance of the contract**.

4 New blacklisted market practices and clauses

Both Royal Decrees respectively add items to the blacklisted trading practices and clauses of Articles VI.109/5 and Article VI.91/4 of the CEL. On the basis of these Articles, if trading practices or clauses qualify as abusive, they will automatically be considered null and void.

The Royal Decree of 4 July 2024

Unfair trading practices relating to delisting products because the supplier asserts legal and contractual rights

The first blacklisted trading practice is related to the prohibition of unfair delisting of the supplier's products. The aim is to prohibit the current practice whereby suppliers are informed that their products will be delisted if they seek to assert their legal or contractual rights. An example of unfair delisting is where the buyer **threatens to delist the products of a supplier if the supplier does not agree to reduce its contractually fixed prices and to align them with the prices of a competitor**.

The Royal Decree also states that the practice of withdrawing or threatening to withdraw agricultural and food products from the shelves, **without informing the supplier in writing beforehand**, must be considered as an aggressive trading practice, prohibited in all circumstances.

The executive power makes very clear that its purpose is **not to restrict the freedom of contract or the possibility for the parties to negotiate**. In other words, this blacklisted trading practice does not prohibit the possibility of delisting products to adapt to consumer preferences or to follow a change in the offers proposed by the supplier. Negotiations between suppliers and purchasers of agricultural and food products relating to their prices are part of the contractual freedom, and the threat of delisting remains a means of exerting pressure that is not covered by this new provision. For example, it will not be considered abusive to remove products from the shelves when the buyer is faced with price increases imposed by a supplier but not justified by their agreement.

This new blacklisted trading practice is a **clarification of Article 109/5, 8° of the CEL**, which already states that trading practices will be considered abusive if they allow the buyer to threaten or retaliate against the supplier "*if the supplier exercises its contractual or legal rights*".

Trading practices allowing for the automatic application of damages

Economically stronger buyers sometimes **automatically charge damages for failure to meet agreed commitments**, such as the time of delivery, insufficient quality of the goods, or damage during transport, without giving their suppliers the opportunity to react. According to the Belgian executive power, this leads to a situation where suppliers have to pay damages **even if they should not be held liable**. In practice, damages are charged automatically by buyers, without justification, and without suppliers being actually liable for the damages caused.

The aim of the Royal Decree is to ensure that buyers can no longer automatically and without prior notice, activate an indemnity clause. The other party must **always be informed** of the reason why damages are imposed or why the indemnity clause in the contract will be activated.

The Royal Decree does **not prohibit indemnity clauses, and does not derogate from Article 5.88 of the Civil Code**. The purpose is simply to ensure that indemnity clauses can only be activated by one party when a non-performance is attributable to the other party. It also follows from the standard requirements that a creditor cannot automatically activate an indemnity clause, but must first provide prior written justification of the contractual non-compliance, justifying the claimed amount.

In other words, the Royal Decree is only reminding and applying the principles enshrined in Articles 5.83 and 5.88 of the Civil Code.

Trading practices allowing the unilateral set-off by the buyer of damages without prior written notification

To protect suppliers against **unilateral and unjustified set-offs between the agreed prices and any damages**, it has been decided to prohibit set-offs when they are made unilaterally and without prior written notification. The requirement for prior written notification from the buyer will also enable the suppliers to contest the application of such set-offs.

Trading practices allowing non-compensatory penalties

Article VI.91/5, 8° of the CEL already states that clauses are presumed unfair if they set "*amounts of damages claimed in the event of non-performance or delay in performance of the other party's obligations which manifestly exceed the extent of the loss likely to be suffered by the undertaking*". Clauses providing for a "private penalty" are thus presumed to be unfair.

However, Article VI.91/5, 8° of the CEL does not prevent suppliers from being faced with the imposition of such "private penalties" by their co-contractors. Therefore, it has been decided to expressly prohibit trading practices allowing penalties that are not compensatory and that are in fact hidden private penalties.

Unlike Article VI.91/5, 8° of the CEL, these trading practices are not presumed to be unfair: in this specific case, **the presumption is merely irrebuttable**.

Applicable sanction

The Royal Decree of 4 July 2024 does not provide for a specific sanction. Therefore, Article VI.109/8 of the CEL applies: unfair trading practices are **prohibited** and the contractual terms embodying the same are void. The contract remains binding on the parties if it can be applied without the prohibited contractual clause. Other sanctions and or remedies may potentially also apply in the context of public or private enforcement.

The Royal decree of 20 June 2024

Terms excessively limiting the liability of the franchisor regarding its delivery obligations towards the franchisee

In contracts concluded between a supermarket chain and one of its franchisees, it is not uncommon for the franchisee to be **exclusively supplied by the franchisor and not to have any adequate exit in case of default of supply of the latter**. Through the Royal Decree of 20 June 2024, the following clauses will be absolutely prohibited:

- Clauses stipulating that the franchisor's delivery obligation is merely a **best efforts obligation**, both in terms of delivery deadlines and quantities to be delivered;
- Clauses using a "**broad**" **definition of *force majeure***: according to some clauses, the mere failure of the franchisor to deliver the goods on time or to deliver non-compliant goods constitute cases of *force majeure*; and
- Clauses subjecting the franchisee to an **indemnity clause if he is supplied by third parties** following a failure of delivery by the franchisor.

However:

- If the absence of delivery directly results from negotiations conducted between the franchisor and its wholesalers, the franchisee cannot be supplied by a third party; and
- If the absence of delivery results from a genuine *force majeure*, the franchisee can be supplied by a third party, but cannot claim compensation from the franchisor.

Terms prohibiting the preparation for or beginning of negotiations during the notice period or within the duration of a non-compete clause

Currently, some confidentiality and non-compete clauses are so broadly worded that the franchisee cannot even begin negotiations or prepare to launch a new business during its notice period, often on the grounds that it would constitute a violation of these clauses. This prohibition applies usually to the launch of new activities whether identical or similar activities.

This situation has also been deemed unfair. Therefore, without prejudice to a valid non-compete clause, a clause preventing the franchisee from negotiating the start of any new business activity with other companies during the notice period or within the timeframe covered by the non-compete clause will now automatically be considered abusive.

Terms requiring the franchisee to bear more than half of the costs of promotional activities

The franchisor sometimes requires its franchisee to implement promotional actions to maintain its market shares. This can be particularly detrimental to the franchisee, who must **comply with this mandatory promotion and often bear the costs alone**. Therefore, the Royal Decree prohibits clauses or combinations of clauses that aim to make the franchisee bear more than half of the costs resulting from the realisation and implementation of promotional sales activities imposed by its franchisor.

Terms requiring exclusive competence of the courts and tribunals of the franchisor's seat or of courts and tribunals located in a different linguistic region than the franchisee's

According to the Royal Decree of 20 June 2024 , terms imposing the exclusive competence of the court of the franchisor's seat or clauses imposing to launch judicial proceedings in another language than the one of the franchisee should be considered as null and void because they further weaken the position of the franchisee in its contractual relationship with the franchisor.

We understand that the new provisions are applicable **without prejudice to Article 624 of the Judicial Code or the Act of 15 June 1935 relating to the use of languages in judicial proceedings**. Consequently, it will still be possible to actually have proceedings in Dutch, even if the franchisee speaks French, or proceedings before the court of the franchisor's seat. What the Royal Decree forbids is to have clauses imposing such situations *beforehand*.

The Royal Decree of 20 June 2024 only targets clauses exclusively relating to the designation of a judge from the judicial order; it does not apply to arbitration clauses.

Applicable sanctions

The Royal decree of 20 June 2024 does not provide for specific sanctions in case blacklisted clauses are discovered in a franchise contract. Therefore, the common sanction of **Article VI.91/6 of the CEL** will apply, namely **the nullity of the unfair term**; the contractual term will automatically be of no effect from the beginning. The judge will then assess the legal position of the parties by **replacing the unfair term with mandatory or supplementary legal provisions that would have applied in its absence**.

Of course, the impact of the nullity on the contract will have to be assessed **on a case by case basis**. The usual course of action is that the judge can replace the nullified term unless, without this term, the equilibrium of the contract is affected. In other words, the contract must be able to exist and be performed even without the unfair term.

In the case of blacklisted clauses targeting non-core obligations, reducing the clause to what is legally permissible should not cause particular difficulties, and should not prevent the contract from existing. However, as mentioned, the Royal Decree of 20 June 2024 sometimes targets the **core obligations of the parties**; in such cases, the nullity of a clause may risk causing **the nullity of the contract as a whole**.

Take, for example, a clause foreseeing that a franchisee cannot be supplied by a third party, even in cases where they are not supplied on time by the franchisor. Such a clause will be considered null and void. Could the contract be performed without this unfair term? This is not certain; if the clause is null and void, there could be no limitation for the franchisee to be supplied by third parties, even if the supply by the franchisor is a core obligation and a core right in the contract. In this specific case, the judge may have to rule that without this particular clause, the contract cannot be performed anymore, leading to its nullity as a whole.

5 New greylisted trading practices and clauses

Both Royal Decrees respectively add items to the list of greylisted trading practices and greylisted clauses of Articles VI.109/6 and Article VI.91/5 of the CEL. Contrary to blacklisted trading practices and clauses, there is only a rebuttable presumption that such clauses or trading practices are unfair, and thus null and void. The parties have thus the possibility to rebut this presumption, so that the clause or trading practice be then valid.

The Royal Decree of 4 July 2024

Trading practices allowing the buyer to pay the supplier a price inferior to the costs of production

Article VI.116 of the CEL states that "*it is forbidden for any company to offer for sale or sell goods at a loss. A sale at a loss is any sale at a price that is not at least equal to the price at which the company purchased the goods or which the company would have to pay when the goods are restocked […]*". This prohibition cannot apply to goods produced in the agricultural and food supply chain, as there is no supply price or replenishment price. The Belgian executive power has therefore decided to introduce a rule according to which **trading practices allowing a buyer to buy goods from his supplier at a price lower than the production costs is presumed abusive**.

The rationale for this new provision is linked to several factors, including the volatility of production costs, which depends on a whole range of factors and circumstances, such as the type of products, farming methods, climatic conditions, pricing factors and the price of feed, which can fluctuate from month to month. In other words, these are **unknown circumstances at the moment of the conclusion of the contract**, that may have a major impact on the costs of production of the supplier. It therefore regularly happens that the agreed price no longer covers the actual production costs.

The Royal Decree aims to avoid such situations. Therefore, clauses permitting the buyer to pay to the supplier a price inferior to his costs of production **will be presumed abusive**. The Belgian executive power consciously chose not to include this trading practice in the list of blacklisted trading practices to allow suppliers the opportunity to sell their products at a loss, especially if that is the only alternative to the destruction of their production.

Two elements must be highlighted. First, the Royal Decree does not define the notion of "costs of production". However, a working group is bringing together representatives of the sectors concerned and economists and is currently in the process of **determining specific production cost indices for each sector**. The purpose is to use these cost indices to determine if a contract or trading practice allows a buyer to pay a price that is lower than the supplier's costs of production.

Second, the Royal Decree specifies that **the costs of production must be determined at the moment of the conclusion of the contract**. In other words, if the production costs increase after the conclusion of the contract, the supplier cannot claim that the buyer purchased their products at a price lower than their actual production costs. While this provides legal certainty to the buyer, it raises questions regarding compatibility with the rationale of this specific greylisted trading practice, as the Belgian executive power has acknowledged that the real problem is the unforeseeable fluctuation of prices ***after*** the conclusion of the contract.

Trading practices excluding hardship

Faced with trading practices that automatically exclude the application of the theory of hardship even when the conditions of Article 5.74 of the Civil Code are met, the Royal Decree aims to add to the list of practices presumed to be unfair; the refusal by one of the parties to renegotiate the contract when the conditions for its performance have changed in such a way that it has become excessively onerous and cannot reasonably be required. In other words, the purpose is to ensure that the parties renegotiate the contract when the conditions for the application of the theory of hardship, as set out in Article 5.74 of the Civil Code, are met.

As pointed out by the Council of State, this is not a blacklisted trading practice, but a greylisted one, which means that the presumption can be rebutted. The presumption can be rebutted if it can be shown that there was **a prior agreement regarding the exclusion of hardship in clear and unambiguous terms between the supplier and the buyer**.

One could wonder what the added value of this new greylisted trading practice is. First, as with the majority of the blacklisted and greylisted trading practices added by the Royal Decree, it merely reflects an already existing provision (Article 5.74 of the Civil Code). Furthermore, if a clause prohibiting the application of the theory of hardship is included in a contract concluded between a farmer and the buyer, it will be difficult for the former to prove that this clause is a greylisted one, based on the Royal Decree, because the condition of "prior agreement" will be met. In other words, one could question how this new greylisted trading practice could, in practice, deter a buyer from restricting the application of hardship in a contract.

The Royal Decree of 20 June 2024

Option or pre-emption right terms with unbalanced valuation of the franchisee's business

Commercial partnership agreements in the food retail sector often include option and pre-emption clauses related to the franchisee's business or shares, benefiting the franchisor. Such a clause is not inherently abusive, except when it results in a **derisory transfer price** that the franchisee must accept because a lump-sum evaluation of their business is provided in the contract. This type of clause will then be considered abusive if it leads to a transfer price significantly below the business' value. In other words, the franchisor can acquire the franchisee's business, but the price must be based on an appropriate evaluation method.

The Royal Decree of 20 June 2024 does not define what is meant by an "appropriate evaluation method" and merely indicates that "*lump-sum valuation clauses are presumed to be unfair when the valuation formula or lump sum results in a clearly unreasonable price considering the market value of the business or shares*". It is expected that many discussions will take place to determine the "manifestly unreasonable" character of the price paid by a franchisor, and that the case law and legal scholars will have to elaborate guidelines in this area.

Clauses contractually forcing the continuation of a structurally loss-making activity

As with any long-term contract, it is obviously undesirable to maintain the franchisee's activity if the business proves to be structurally loss-making for various reasons. Nonetheless, the franchisee is sometimes contractually obliged to continue its loss-making activities under threat of payment of damages in case of early termination. Therefore, it should be possible for a franchisee to terminate its commercial partnership agreement with a **maximum notice period of four months in case of structurally loss-making activity**.

The concept of "structurally loss-making" has not been precisely defined by the executive power: its goal is to maintain an open definition, allowing a case-by-case approach.

Clauses allowing the franchisor to terminate the commercial partnership agreement in case of sufficiently serious non-performance by the franchisee

Commercial partnership agreements in the food retail sector often provide a termination clause allowing the franchisor to terminate the contract by registered letter immediately or within an excessively short period (e.g. 48 hours) following a formal notice of default, in case of sufficiently serious non-performance by the franchisee.

However, commercial partnership agreements require the franchisee to make significant investments. Given the importance of these investments, contracts are generally concluded for several years. Thus, it does not seem balanced for the franchisor to be able to terminate the contract on such short notice. Considering the serious consequences such termination may have on the franchisee, the Royal Decree of 20 June 2024's preparatory works indicate that termination clauses are prohibited: **it is, therefore, up to the judge to decide if a serious breach justifies the contract's termination**.

The wording of the Royal Decree's preparatory works is unclear regarding this prohibition on termination clauses. The Belgian executive power first targeted termination clauses allowing **immediate or extremely brief termination**. Yet, a few lines later, it is stated that **the application of termination clauses is prohibited, and it is up to the judge to decide if the franchisee indeed committed a serious fault**. It will be up to the legal scholars and case law to resolve this ambiguity. Furthermore, as phrased, the Royal Decree suggests that this clause should be considered a blacklisted clause, not a greylisted one.

Questions may also arise regarding the interactions between this type of greylisted clause and the common rules of Book 5 of the Civil Code relating to termination of contracts. As a reminder, Article 5.93 of the Civil Code provides for the possibility for the creditor to terminate the contract by means of unilateral notification in case of serious default by its debtor. By only targeting termination clauses without limiting or excluding the right provided for by Article 5.93 of the Civil Code, the Royal Decree might miss its objective of protecting the franchisee from abrupt termination of the franchise agreement.

In any case, attention must also be paid to the case law developed on the matter: if the application of termination clauses (on short notice) is prohibited, it remains to be determined how the franchisor and franchisee will maintain their contractual relations during the entire judicial procedure, both in the first instance and on appeal.

6 Application in time of the Royal Decrees

The Royal Decree of 4 July 2024 entered into force on 1 October 2024 and is applicable to supply agreements entered into, renewed or amended after that date. The Royal Decree of 4 July 2024 will be applicable to existing supply agreements as of 25 January 2025.

The Royal Decree of 20 June 2024 will enter into force on **1 January 2025**. It will first apply to all commercial partnership agreements concluded, renewed, or modified after this date. In a second phase, the Royal Decree of 20 June 2024 will also be applicable to **all commercial partnership agreements** falling withing the scope of the Royal Decree from **1 May 2025**.

It is therefore high time for those targeted by these Royal Decrees to review their existing agreements and make the necessary changes.

Feel free to reach out to your usual contacts if you would like to discuss the topics covered in this newsletter further.