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Criteria used by the Belgian Courts to calculate the indemnities for distributors under the law of 1961

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1. Introduction

1. Belgium has a specific law concerning the termination of distribution agreements, the law of ***27th July 1961*** which consists of ***mandatory rules***.

This law, in comparison with other countries, is ***particularly protective*** of the distributor, especially with respect to the calculation of the indemnity in lieu of notice and the goodwill-indemnity. However the law of 1961 does not fix the minimum or maximum amount of these indemnities. Therefore the courts settle this amount equitably, taking into consideration the particular circumstances. In practice the courts are guided by commercial customs and by valuable classic criteria.

2. As far as jurisprudence is concerned, it should be pointed out that recently the position of the Belgian courts has changed, mostly regarding the definition of a reasonable period of notice. Indeed the courts currently do not only take into account the interest of the distributor but also that of the supplier. Consequently the amount of the indemnities will probably be reduced.

2. Reasonable notice period and indemnity in lieu of notice

3. Under article 2 of the law 1961, either party can terminate a contract made for an indefinite period giving a ***reasonable notice period*** or a ***fair compensation*** to be agreed upon between the parties, unless there has been a serious breach of duty.

The definition of a "reasonable notice period", according to doctrine and case law, has recently been developed. Previously a reasonable period of notice corresponded with the period which was, in theory, necessary to enable the distributor to enter into a similar distribution agreement. This *classic interpretation* complies less and less with the current economic situation; indeed nowadays it might be difficult for a distributor, after termination of the agreement, to find another distribution agreement that is equivalent. Therefore the courts have *recently* settled a new definition of a reasonable notice period which not only takes into consideration the interest of the distributor but also that of the supplier.

In this respect the Court of Appeal of Brussels (1st April 2003) stated that "*there is a reasonable notice period when, at the moment of termination of a distribution contract, a period necessary to find an equivalent source of income is granted to the distributor. There is no necessity to find a new distribution agreement covering the same or equivalent product*".

In another case the Court of Appeal of Brussels (21st March 2003) decided that "*the reasonable notice period has to be sufficient to allow the distributor to fulfil his duties towards third parties and to obtain a net income equivalent to the lost income, if necessary with a total or partial reconversion of its activities*".

This decision has been confirmed by the Supreme Court (*Cour de Cassation - Hof van Cassatie*) (10th February 2005), which stresses that *"the aim of the legislator is to provide the distributor with a period which is necessary for reorienting his activities, in order that the distributor does not become ruined because of the termination of the distribution agreement*".

Therefore, according to case-law (Court of Appeal of Brussels, 21st March 2003, Court of Appeal of Brussels, 29th June 2001), the reasonable notice period currently has to be fixed ***in equity, taking into consideration the interests of both the parties***.

4. This interpretation is consistent with the actual aim of the Law of 1961 which is to protect the distributor, without compromising the legitimate interest of the supplier. In this way indeed the courts underline that "*the distributor has no right to remain a distributor for life*" (Court of Appeal of Brussels, 21st March 2003) and that "*the distributor cannot demand a notice period necessary to enable him to find a distribution agreement which provides for equivalent effects to those of the lost agreement*" (Court of Cassation, 10th February 2005); indeed, as decided by the Court of Appeal of Antwerp, 19th September 2002, "*the burden of finding an equivalent distribution agreement shall not be a disadvantage for the supplier only*".

5. With a minimum notice period not being required by Belgian law, a reasonable notice period shall be agreed by the parties at the moment the notice is sent. If the parties cannot agree on the notice period, the courts will settle the matter equitably, taking into consideration the particular circumstances. In practice when setting the real term of the notice period the courts are guided by commercial customs and by valuable classic criteria, such as f.ex.:

- duration of the agreement;
- extent of the territory and the number of clients and other advantages linked to the agreement;
- percentage of the distribution activities in the global activity of the distributor;
- development of the turnover during the agreement;
- renown and specificity of the supplier's products and the possibility of selling similar products or replacing the distributorship;
- complexity of the organisation and the obligations assumed by the distributor in order to perform the contract;
- investments.

As far as these criteria are concerned, according to the above-mentioned new interpretation of "reasonable notice period", case-law (Court of Appeal of Brussels, 21st March 2003) confirms that it is necessary to take into account the classic criteria and, in addition, it points out that "*all criteria useful for settling the notice period necessary for total or partial reconversion of a distributor's activity need to be considered*".

Therefore it is important to determine the *percentage of the distribution activities in question within the global activity* of the distributor; indeed if the distributor has already developed other accessory activities beyond the distribution activity in question, it would be easier to carry out a reconversion of the activity.

6. In practice, case-law shows that the notice period granted by the courts can vary enormously, depending on the particular circumstances. In fact, the decisions on this vary ***between 1 and 42 months***.

However, according to the new interpretation of a "reasonable notice period" settled by Court of Cassation (10th February 2005), the term of such a period probably would be shortened; indeed, as mentioned before, a reasonable period notice is not the period which is necessary to enable the distributor to find an equivalent distribution agreement, but that of obtaining a net income equivalent to the lost income.

7. If the notice period granted is considered insufficient, the courts shall decide in equity the amount of the indemnity.

On the contrary, whenever the terminating party chooses to give to the other party an indemnity instead of the notice period, but they cannot agree the amount of this indemnity, the courts as well shall decide the matter in equity.

However, concerning the choice between a minimum period of notice or payment of an equivalent sum of money, according to the Court of Cassation (4th December 2003) "*the obligation to pay an indemnity is not an autonomous contractual obligation, but an obligation which replaces a contractual obligation to respect a reasonable period of notice whenever that is not respected*". According to this case law, the terminating party's duty of giving a reasonable notice period or a fair indemnity would not be considered as an alternative obligation.

However it needs to be pointed out that the majority of the Belgian doctrine considers that this interpretation is not in compliance with the text of art. 2 of the Law of 1961. Indeed, to settle that the payment of a fair indemnity would not be considered as an autonomous obligation is as if to deny the existence of the choice for the terminating party; on the contrary, this choice is clearly fixed by the law. In practice, according to the doctrine and to the text of art. 2 of the law of 1961, the terminating party can opt for the indemnity, without granting a notice period.

8. The indemnity should only correspond to the profits the other party would have enjoyed during the term of notice, if it had been given, and the courts tend to respect this principle (Comm. Bruxelles, 7th June 1989. Bruxelles, 15th March 1990; Comm. Bruxelles, 29th March 1990; Comm. Bruxelles, 5th October 1994, Comm. Gand, 25th January 1996).

In practice, the courts proceed using the following *two different methods of calculation*: the indemnity is equal to the ***net profit*** which the distributor would have enjoyed if a reasonable notice period had been given, ***increased by the irreducible overheads*** up to the percentage represented by the distributorship in the total turnover of the distributor for the same period (Bruxelles, 4th December 1986; Anvers, 8th march 1988; Comm. Bruxelles, 31st January 1986; Bruxelles, 7th march 1991); the indemnity is equal to the ***gross profit*** which the distributor would have achieved if a reasonable notice period had been given ***after deduction of the reducible overheads*** directly related to the distributorship (Bruxelles, 15th March 1990; Comm. Bruxelles, 13th June 1997).

"Irreducible overheads" means the costs which remain to be paid independently of the continuation of the distribution, while "reducible overheads" means the costs which can be directly linked to the products of the distribution agreement and which disappear when the products are no longer sold.

The calculation of the indemnity takes into consideration the average profit (net or gross as explained above) made by the distributor *during the last 2 to 3 years of the distribution* agreement. This average would be multiplied for the months of the period of notice which was due and was not respected.

9. Generally the majority of the courts (Court of Cassation, 25th March 1976, Court of Appeal of Brussels, 21st March 2003, Court of Cassation, 4th December 2003) take into account the period of activity preceding the termination of the agreement only, and not the possible period of notice also.

Part of the Belgian doctrine considers this interpretation the only one in compliance with the text of art. 2 of the Law of 1961 which settles that the parties fix the reasonable notice period or the indemnity at the moment the notice of termination is sent.

However, recently, the Court of Cassation (16th May 2003) decided that "*neither the fact that the indemnity due to the distributor is fixed by the parties at the moment the notice of the termination is sent, nor the equity on the grounds of which the judge has to decide, may prevent that, when setting the indemnity, the judge consider all the facts that he is aware of at the time of making the decision; it means that he can also take into consideration what the distributor has obtained during the period in which the termination of the agreement was carried out, this includes the period of notice, provided that the termination has not affected his activity*". In the comment of this judgment the attorney general underlines that "*if the right of indemnity arises at the time of the notice from the terminating party, the damage has to be calculated at the moment closest to the effective reparation of the damage, i.e. at the time of the decision (...); the judge has to set the indemnity in the most equitable way possible (...); it would not be equitable to set the amount of the indemnity, that the supplier has to pay, in abstracto, that is according to the average profit gained during the period before termination, if in concreto the damage had been affected by different events following the termination, such as the behaviour of the distributor*".

The Court of Cassation (7th April 2005), in a case concerning the reasonable period of notice, also decided in the same way. In addition the Court declared that the reasonable notice period or the indemnity has not to be decided upon according to an evaluation in abstracto, however according to an evaluation in concreto. That means, as the Court explains, that the ***circumstances following the termination of the agreement can affect the decision*** of the judge, for example that the distributor, during the period of notice, has refused a proposal concerning distribution of another brand of the same product or that the distributor was not very active in the search for other distribution agreements or, on the contrary, has found a new agreement immediately. Therefore the courts, in making their decision concerning a reasonable notice period of indemnity, may be guided not only by the classic criteria mentioned above but also by considering the particular circumstances following the termination of the agreement, such as the behaviour of the distributor and the concrete possibility or chances of finding another distribution agreement.

However, it needs to be pointed out that part of the Belgian literature considers that this new interpretation by the court does not offer sufficient legal certainty; indeed the judge who takes into account the period following termination of the agreement is considering circumstances which the parties cannot have been aware of at the time of the termination. However, according to the literature, the judge when fixing the reasonable period of notice or the indemnity, has to put himself in the supplier's place and take into consideration all facts that he would be aware of at the moment of the termination. If the judge considers the subsequent period also, he changes the real position of the parties. In addition it has to be underlined that the circumstances following termination can be manipulated by the parties and may not be in compliance with reality.

10. In practice the courts, in their decision concerning a reasonable notice period or an indemnity, have above all to ***take into account the facts and have to decide equitably***. This means that it is possible for the judge to also take into consideration what the distributor has obtained during the period of notice, but that does not mean that the judge is obliged to do so.

The courts must decide equitably, according to the particular circumstances of each case. For example the Court of Cassation (4th December 2003), in its evaluation of the indemnity, does not take into account the real costs supported by the distributor during the period of notice, but decides in abstracto.

In conclusion, the majority of Belgian literature uses the evaluation in abstracto, this means only the period of activity preceding the termination of the agreement, as a general rule and the evaluation in concreto, i.e. the period following the termination of the agreement also, as an exception. However the equity and the real facts have always to guide the judge in each case.

3. Goodwill indemnity

12. It must be pointed out that the right to a goodwill indemnity is ***completely separate*** from the above mentioned substitutive right to an indemnity in lieu of notice. Indeed these two indemnities have different aims: the substitutive indemnity has as the aim to compensate the reasonable notice period not awarded, while the supplementary indemnity's aim is to compensate all other financial consequences of termination of the agreement. In addition these indemnities are reciprocally ***autonomous***, that means that one indemnity is not conditioned by the other.

According to article 3 of the law of 1961 the distributor and only the distributor has the right to a so-called "supplementary indemnity" exclusively if and when the following conditions are met:

- the terminated agreement falls within the scope of article 1 of the law of 1961 and
- the terminated agreement was a contract for an indefinite period and
- the agreement is terminated by the supplier for reasons other than serious breach or the distributor terminates the agreement because of a serious breach of the manufacturer.

The amount of this indemnity is calculated on the basis of all the relevant circumstances and, in particular, taking into consideration:

- any substantial increase of the clientele which has been created by the distributor and which remains attached to the supplier after the termination of the contract (goodwill indemnity in the stricter meaning);
- all expenses incurred by the distributor in furtherance of the distributorship which will benefit the manufacturer after the termination of the contract;
- the amounts to be paid by the distributor to the employees he or she is obliged to make redundant as a result of the termination of the distributorship.

In any case, neither does the law nor jurisprudence provide any minimum or maximum amount of this compensation. Moreover, being the factual circumstances are to be taken into consideration, the outcomes of the various decisions of the courts are really difficult to foresee and it cannot be held that there is an amount generally recognised by the court. Case law shows that indemnities ***between 6 months of net profit and 24 months of gross profits*** have already been recognised.

13. Concerning the goodwill indemnity in the strictest meaning, (clientele indemnity), the distributor has to prove that three conditions are satisfied. Recently jurisprudence has clarified this indemnity and these conditions.

As concerns the ***substantial increase of clientele***, normally this increase has to be calculated using a comparison between the clientele at the beginning of the distribution agreement and the clientele at the end of the agreement. However it is not always so simple to determine the size of the clientele at the beginning of the distribution activity, especially when the agreement has lasted for a long time. Normally in this last case the Court presumes that there was an increase. The conclusion is the same in the case where the distributor is the first distributor of this product in this territory. Indeed, if previously there was no distribution in this sector, it is normal to presume that the clientele was created by the initial distributor. The Court of Cassation, 7th January 2005, decided that the judge is not required to determine the increase of the clientele using a comparison between the clientele at the beginning of the distribution agreement and the clientele at the end of the agreement; the judge can assess simply according to the circumstances of the case, that there has been an increase.

Concerning the second condition that the increase of the clientele has been ***created by the distributor***, it is not necessary that the distributor proves his merit in the increase of the clientele but it is sufficient that he proves that he has contributed to the realization of the increase in clientele. However this condition is not proved by the simple and normal management of the distribution activity.

Concerning the last condition, i.e. the clientele ***remains attached to the supplier*** after termination of the contract, there are two different opinions:

1. according to the first opinion, the fact that the clientele remains with the supplier must be evaluated in abstracto, i.e. that it is sufficient to verify the possibility that the clientele is faithful to the supplier;

2. according to the second opinion this evaluation has to be made in concreto since it is an economic reality.

The most important difference between these two interpretations is that, according to the first opinion the evaluation in abstracto is only up until the moment of termination of the agreement, whereas according to the other opinion the evaluation in concreto requires that the period after the termination is also taken into consideration, thus also the period of notice.

With regard to this question, as mentioned before, the Court of Cassation recently (10th February 2005, 7th April 2005) stated that, according to equity, the judge can take into consideration all the facts that he is aware of at the moment of the decision, such as the situation of the distributor following the termination of the agreement; the Court specifies also that anyway the judge is not obliged to do this evaluation in concreto.

However it must be pointed out that, concerning the goodwill indemnity in general, this evaluation in concreto is the only one in compliance with the text of art. 3 of the Law 1961; indeed unlike art. 2 of the Law of 1961, art. 3 does not state that the parties fix the supplementary indemnity at the moment the notice of the termination is sent. On the contrary, according to art. 3, the circumstances that have to be taken into consideration also concern the period following the termination of the agreement. Indeed art. 3 always mentions the substantial increase in the clientele, the expenses and the amounts paid to the employees with reference to the period following termination of the contract.

Furthermore, the Courts normally, in the evaluation of the third condition of the clientele indemnity (i.e. the clientele remains attached to the supplier after termination of the contract) attach importance to ***trademarks*** of the distribution's products. When the distributor sells the products, during a distribution agreement, under his own trademark, the judge presumes that the clientele remains loyal to the trademark, thus the distributor will not be entitled to receive a supplementary indemnity for the clientele. On the contrary when the products are sold under the trademark of the supplier, it is normal to presume that the clientele remains loyal to the supplier.

4. Conclusion

14. When taking the above into account, it is clear that the Belgian legislation, in spite of the recent approach taken by the courts, remains especially protective of the distributor. In addition it must be pointed out that with the law of 1961 being a so-called "*loi de police*" or '*loi d'application immediate*", the mere choice by the parties to opt for another country's law will not be sufficient to avoid that a Belgian judge would apply Belgian law to a distribution contract executed in Belgium. Therefore in order to avoid the application of the Belgian law, it is necessary to agree a jurisdiction clause in favour of foreign courts.

On the contrary the arbitration clauses are not sufficient to avoid Belgian law because they will be applicable only when they provide for the application of the Belgian law by the arbitration court.

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