



## IDI CONFERENCE

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### **First case study: Terminating a contract because the distributor is selling competitive products.**

Background: An agency contract contains a clause according to which the agent undertakes not to represent any competing products. The agent represents since several years a competing product. There is evidence that the principal has always been aware of this and has tolerated this fact because the representation of competing products has not affected the sales of the contract products. Recently, the principal found another agent and would like to terminate the contract for cause.

The panelists have been requested to comment on the situation on the basis of their domestic laws.

First of all, it is necessary to give the basics of the Finnish legal system. Finland is a civil law country, and the roots of its contract law are Scandinavian and German.

There is no special legislation in Finland concerning distributorship agreements whereas agency is covered by legislation implementing EC Directive.

Finland has no comprehensive civil code like the German BGB or the French Code Civil. The general principles of contract law are not codified, which makes case law and doctrine important as sources of law in the field of contract law.

General contract law principles of Finland, as well as the other Nordic countries, know the doctrine of good faith and fair dealing, usually referred to as the principle of loyalty and the principle of fairness. In Finland, the principle of loyalty has been recognized in a few judgments from the Finnish Supreme Court, the first one of them was given in 1993. None of these cases expressly covers agency and distributorship contracts, but it is evident that these contracts and parties thereto are subject to the principle. The underlying idea is conceive a contractual relationship as a cooperative project for the parties instead of an arrangement which entitles a party to pursue only his or her own interests.

The principle of loyalty also generally limits a party's right to invoke written contractual clauses to the detriment of the other party. However, this effect of the said principle should be seen as an exception rather than a rule.

Finland has implemented Directive 86/653/EEC already before its EU membership in 1992 through the Act 417/1992 on Commercial Agents and Salesmen (the Agency Act). Notable in the Act is section 3, which provides that written form may be requested by either party for the conclusion and amendments of an agency contract.

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The question posed to the panelists leaves out the question of choosing another law to govern the relationship. The above Act states that parties cannot derogate from the provisions of the Act protecting agents by choosing another law to govern the contract.

#### **A) TERMINATION OF THE CONTRACT WITHOUT NOTICE UNDER ARTICLE 19, INVOKING THE BREACH OF ARTICLE 3**

Section 25 of the Act lists reasons for an immediate termination of an agency agreement. The list contains examples of conduct due to which a party cannot reasonably be expected to pursue a relationship with the other party.

Item 3 of paragraph 2 of section 25 mentions as a cause "a conduct seriously violating the other party's interests or otherwise causing the loss of trust to the violating party". Item 4 section refers to fundamental breach by a party of its obligations under the contract.

Articles 3 and 19 of the contract in question would in my view constitute valid grounds for immediate termination under Finnish law.

However, paragraph 3 of Section 25 of the Agency Act requires the violated party to exercise his rights without unreasonable delay after he has become informed of the cause. In the circumstances of this case, Futura Spa would therefore have lost its right to immediate termination.

Futura could nevertheless terminate with immediate effect but would have to compensate the losses sustained by Müller.

One can ask to what extent are the above provisions mandatory. It is only stated that an agent cannot effectively waive his rights of compensation due to the unjustified termination. Since reference is made to the provisions of section 25, it can be concluded that the grounds and the time limit for termination are mandatory.

#### **B) ASKING THE AGENT TO STOP DISTRIBUTING THE MARLENE JACKETS WITHIN 15 DAYS AND TERMINATING THE CONTRACT FOR BREACH IF HE DOES NOT**

The first issue to notice here is that this scenario does not make much difference with the previous one with immediate termination. The agent cannot effectively change its business plan in 15 days without significant effects on its revenues but can only terminate the other agencies, potentially with sanctions under the relevant contracts.

Section 36 of the Finnish Contracts Act makes it possible to disregard or adjust unfair contracts. There is also a prohibition of chicanes (using the legal powers effectively to the detriment of the other party). One can conclude that it is impossible to circumvent Section 25 paragraph 3 of the Act on Commercial agents by using this construction. .

Finnish law like other civil law countries recognizes the principle of *venire contra factum proprium* which is an equivalent of estoppel in Anglo-American law. The application of this principle is in accordance with the principle of loyalty or good faith and fair dealing.

Here we are dealing with a universal legal principle. We may recall what Article 1.8 of the UNIDROIT Principles for International Commercial Contracts 2004 states

*A party cannot act inconsistently with an understanding it has caused to the other party to have and upon which the other party reasonably has acted in reliance to its detriment*

This principle largely corresponds also with the Finnish civil law doctrine. More technically, passivity can have constitutive effects under Finnish contract law, which is reflected in a number of provisions in the Finnish Contracts Act which governs primarily formation of contracts.

There is also a notice requirement under general contract law principles for a breach of contract within a reasonable time from the time the violated party became aware of the breach. The principle has found effect in paragraph 3 of section 25 of the Finnish Agency Act. If this is not complied with, a remedy is lost.

One can refer to an oral agreement or practice between the parties to amend a written contract or even to contradict it. However, the burden of proof as regards acting in contradiction with a written contract on the basis of the conduct of the other party must be on the party relying on it.

The Finnish Act on Commercial Agents and Salesmen makes it possible to agree that written form is exclusive in amending a contract. If such a provision is included in the contract, it is more difficult, but not necessarily impossible, to invoke the conduct of the other party as an amendment to the contract.

#### **WOULD THE RESULT BE DIFFERENT IN THE PRESENCE OF A NON-WAIVER CLAUSE?**

A clause, according to which failure by a party to exercise a right or remedy does not constitute a waiver thereof is valid under Finnish law. However, such a clause is invalid if it would allow disloyal behavior by a party invoking it. An example of a disloyal conduct would be an exercise of a right or remedy for reasons other than the avoidance of detrimental effects of the breach. In this case, Futura wants to enter into a more profitable relationship with another agent and probably could not therefore invoke a non-waiver clause.

It may also be concluded that a failure to invoke a termination within a reasonable time in accordance with section 25 paragraph 3 of the Agency Act would also bar the exercise of termination without a duty to pay damages irrespective of a non-waiver clause. In case we were talking about distributorship, the solution might be different.