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Contractual Networks and the Small Business Act:  
Towards European Principles?

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DEPARTMENT OF LAW**

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Towards European Principles?*

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## **Abstract**

In this paper, I address the issue of contractual networks in the European context. The term “contractual networks” encompasses both multilateral contracts and networks of linked bilateral contracts. Contractual networks are hybrid forms of organisation located between markets and hierarchies. Networks differ from market contracts because the participants are not impersonal agents, but well identified players chosen on the basis of resource complementarities. They permit resource bundling that markets are unable to achieve. They differ from hierarchies because enterprises are autonomous and legally independent even if they may be economically dependent. The main characteristics of contractual networks are: interdependence, stability of relationships, long-term duration and multiplicity. Moreover, competition can also supplement cooperation as partners can cooperate on some projects whilst competing in other ways. The increasing importance of networks at EU level forces us to rethink two main policy issues: 1) how, and according to which variables, important is it to distinguish between contract and company law in relation to inter-enterprise coordination; 2) how to regulate multilateral contracts among enterprises. So far, contractual networks have not been adequately recognised at European level where, at least implicitly, the traditional partition between exchange and organisational contracts has held firm. The Council asked the European Commission to define a new framework for small and medium enterprises (SMEs), and the latter recently launched a program to draft a Small Business Act which will include a company law statute for SMEs. Despite the inattention of both European contract law drafters and private international law, networks, especially those among SMEs, have gained momentum in policy-making. The ever more frequent references to networks, both contractual and organisational, in relation to policies associated with competitiveness and growth suggest that it may be necessary to coordinate with the governance dimension associated with their private law regimes. The paper suggests that Principles of European contractual networks (PECON) are defined and coordinated with the current DCFR. I sketch some of the possible guiding ideas and the necessity of coordinating substantive principles with private international law principles pursuant to the ROME I Regulation. It also proposes that the forthcoming Small Business Act should incorporate guidelines concerning contractual networks, be they domestic or transeuropean.

## **Keywords**

Contract – Network - Contractual interdependence - Business Act - Common Frame of Reference - multi-lateral contracts - linked contracts - Consortium.

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# *Contractual Networks and the Small Business Act: Towards European Principles?\**

Fabrizio Cafaggi

## **I. Introduction**

In this paper, I address the issue of contractual networks in the European context<sup>1</sup>. This term encompasses both multilateral contracts and networks of bilateral linked contracts<sup>2</sup>. Contractual networks are hybrid forms of organisations located between markets and hierarchies<sup>3</sup>. Networks differ from market contracting because the participants are not impersonal agents but well identified players chosen on the basis of

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\* This essay is part of a wider research project within REFGOV, a 6<sup>th</sup> framework research program. A shorter version will be published in issue 4 of European contract law review 2008.

Many of these ideas have developed discussing within a research group in Trento. I am grateful to all participants in that group for stimulating discussions. The research material is available on the web site [www.dieresi.it](http://www.dieresi.it).

I thank Stefan Grundmann, Paola Iamiceli, Giesela Ruhl, and Simon Whittaker for stimulating conversations, John Armour, Simon Deakin and Katharina Pistor for useful comments to a presentation given in Cambridge UK, December 2007. Excellent research assistance was provided by Federica Casarosa, Chiara Ferrari, Marco Gobbato, Stefano Montemaggi, Florian Moslein. Thanks for editorial assistance provided by Rory Brown. Responsibility is my own.

<sup>1</sup> In a joint project I engage into a comparative analysis with US Contract law. See F. Cafaggi, 'Contractual networks in Europe and US'. While I believe that the concept of network can have a legal dimension, I share the view that is strongly indebted to economic and sociological literature. See below text and fn ...

<sup>2</sup> See F. Cafaggi, 'Reti contrattuali e contratti di rete: ripensando il futuro', in F. Cafaggi and P. Iamiceli (eds), *Reti di imprese tra crescita ed innovazione organizzativa*, (Bologna: Il Mulino, 2007), 413 and before F. Cafaggi (ed.), *Reti di imprese tra regolazione e norme sociali*, (Bologna: Il Mulino, 2004).

<sup>3</sup> See O. Williamson, *Markets and hierarchies: Analysis and antitrust implications*, (New York: Free Press, 1979); O. Williamson, 'The economics of governance', *American Economic Review*, 2005, 1; W.W. Powell, 'Neither markets nor hierarchy: network forms of organisation', in L.L. Cummings and B. Shaw (eds), *Research in organisational behaviour*, (Greenwich: JAI Press, 1990); C. Menard, 'The Economics of Hybrid Organizations', *Journal of Institutional and Theoretical Economics*, 2004, 3, 345; D. Campbell, H. Collins, J. Wightman, *Implicit dimensions of contract: discrete relational and network contracts*, (Oxford: Hart, 2003); A. Schwartz and R.E. Scott, 'Contract theory and the limits of contract law', *Yale Law journal*, 2003, p. 541; G. Teubner, 'Coincidentia oppositorum: Hybrid networks beyond contract and organisations', 2006, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=876939](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=876939); V.P. Goldberg, 'Risk Management in Long-Term Contracts', *Columbia Law and Economics WP*, available at SSRN: <http://ssrn.com/abstract=805184>.

resource complementarities<sup>4</sup>. They permit resources bundling that markets are unable to achieve. They differ from hierarchies because enterprises are autonomous and legally independent even if they may be economically dependent<sup>5</sup>.

They exist in the production stage, i.e. subcontracting, consortia, EEIG, and in the distribution chain, i.e. agencies, franchises, dealerships, and multiple licensing, but also may take the form of collective ownership of trademarks. They emerge when enterprises coordinate economic activities with a high degree of interdependency. I concentrate on interdependencies among enterprises that take network forms. But contractual networks exist in businesses to consumers (BtoC) relationships as well<sup>6</sup>.

Contractual business networks are characterized by interdependence, stable relationships, with long-term duration and multiplicity<sup>7</sup>. (1) Interdependence implies that there is a common goal or set of objectives to be achieved among all participants and that one contract or contractual performance is made dependent on others either unilaterally or reciprocally (2) The **stability** refers to the overall network, not necessarily to individual relationships which may be more or less numerous. A contractual network can be stable even if there is a high degree of entry and exit by individual components. (3) The **duration** of individual relationships among enterprises is relevant, but not a decisive element in identifying a network. Network are characterized by long-term relationships.(4) **Multiplicity**. The number of relationships is also a relevant component in the configuration of a network. Enterprises belonging to a contractual network tend to have multiple relationships; some formal, some informal. Informal relationships take different forms in relation to technological innovation that permits the creation of technological platforms to define memberships<sup>8</sup>. To be sure, to constitute a network only a web of legally binding contractual relationships is needed but the interplay with informal relationship may be extremely relevant for institutional design. (5) **Combination of cooperation and competition**. In contractual networks, partners can cooperate on some projects and compete over other dimensions.

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<sup>4</sup> On the distinction between market and hybrids contracting see O. Williamson, 1979, Id. 2005

<sup>5</sup> 'Hybrids exist because markets are perceived as unable to adequately bundle the relevant resources and capabilities while integration in a hierarchy would reduce flexibility by creating irreversibility and weakening incentives', in C. Menard, 'The economics of hybrid organisations', cit., p. 351. But see B. Klein, 'Vertical integration as organisational ownership: the Fisher Body-general motors relationship revisited', in S. Masten, (ed.), *Case studies in contracting and organisations*, (Oxford: OUP, 1996), p. 199, claiming that vertical integration entails higher degree of flexibility than long-term contracts.

<sup>6</sup> See Research Group on the Existing EC Private Law (Acquis Group), *Principles of the Existing EC Contract Law (Acquis Principles) - Contract I*, (Munich: European Law publisher, 2007), 186 ff. See Article 5:106 based on art 6(4) of the Distance selling directive 97/7, on art 6(7) of the Financial services distance selling directive 2002/65, and on art 7 of the Time share directive 94/47. The article states: '(1) If a consumer exercises a right of withdrawal from a contract for the supply of goods or services by a business, the extent of withdrawal extend to any linked contract. (2) Contracts are linked if they objectively form an economic unit'.

The question of linked contracts has been examined by ECJ in the consumer context see C-350/03 *Schulte v Deutsche Bausparkasse*, [2005] ECR I-09215; and C-229/04 *Crailsheimer Volksbank eG v Klaus Conrads and Others*, [2005] ECR I-09273.

<sup>7</sup> See P. Iamiceli, 'Le reti di imprese: modelli contrattuali di coordinamento', in F. Cafaggi (ed.), *Reti di imprese tra regolazione e norme sociali*, cit., 125.

<sup>8</sup> See F. Casarosa, 'Le reti nella rete – Spunti e riflessioni sull'operatività di Internet fra le imprese', in F. Cafaggi (ed.), *Corporate governance, networks e innovazione*, Cedam, 2005, 75.



Contractual networks require an institutional environment where fiduciary relationships can arise, and also a high level of trust that can allow the development of shared innovative knowledge. They boast, if appropriately designed, comparative advantages in fostering production and transfer of competitive knowledge. Cognitive contractual networks seem particularly suitable to generate innovation. The density of relationships allows more intense production and transfer of competitive knowledge among the components because the network form provides at the same time more incentives to produce innovative knowledge and more safeguards from opportunism (i.e. private use of collective goods).

Contractual networks are often complemented by company networks for different purposes: to stabilise relationships, to establish a separate entity, to facilitate the conclusion of contracts with third parties, to shield network participants from unlimited liability. I will consider the company law dimension not as an alternative to but only where it complements contractual networks<sup>9</sup>.

Contractual networks may emerge in different ways. Some arise as a form of collaboration among independent and autonomous enterprises that decide to increase levels of coordination and interdependence. This frequently happens when enterprises own complementary critical resources and capabilities, but integration through M.A. is not a feasible or desirable alternative because it would bureaucratize the ‘newco’, quickly confounding the advantages generated by the merger. In particular, interdependence leading to contractual networks may be generated by knowledge systems characterized by fragmentation and difficulty to ‘propertize’.

Other contractual networks may be the outcomes of outsourcing. Vertically integrated firms may decide for costs-associated reasons to outsource some phases to other enterprises which already exist in the market or whose creation is promoted by the outsourcers<sup>10</sup>. Only when outsourcing is characterised by a permanent or very stable relationships between the outsourcer and the sub-contractor, not driven entirely by economic dependence of the latter, one should speak of a contractual network. Most frequently these networks combine outsourcing and delocalisation and generate transnational contractual networks (core firms in Italy that delocalise enterprises in Roumania, Balkans, Baltic republics or south east Asia<sup>11</sup>).

The degree of hierarchy and the market power of each enterprise within the contractual network may vary substantively, and this variation poses different governance problems to be solved with appropriate contractual designs. I shall indicate which issues are posed by hierarchy in different models of networks.

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<sup>9</sup> For an analysis of the alternative between contractual and organisational networks, see F. Cafaggi, ‘Il governo della rete’, in F. Cafaggi (ed.), *Reti di imprese tra regolazione e norme sociali*, cit., 57.

<sup>10</sup> D. Mowery and N. Rosenberg, *Technology and the pursuit of economic growth*, (Cambridg, MA: Cambridge University Press, 1989); C. Trigilia, *Sviluppo locale – Un progetto per l’Italia*, (Bari: Laterza, 2005), 49. On the evolution of the different forms of enterprises see F. Amatori, ‘Forme di impresa in prospettiva storica’, in S. ZAMAGNI (ed.), *Imprese e mercati*, Utet, Torino, 1991, 123.

<sup>11</sup> See G. Gereffi, J. Humphrey and T. Sturgeon, ‘The Governance of Global Value Chains’, *Review of International Political Economy*, 2005, 12,1, pp. 78-104.

## II. Contractual Business Networks in the European Union

Contractual business networks constitute, together with pyramidal groups, one of the most diffused forms of organisation at EU level. When these networks involve enterprises located in several MSs, their legal regime is often defined by reference to one or more legal systems, which widely differ. There is no private international law provision specifically addressing contractual networks and the new Regulation, 'Rome I', does not include a specific regime for trans-European contractual networks. The recent draft of the Common Frame of Reference (DCFR) does not regulate contractual networks in the general part, i.e., Book II and Book III, while references to networks are made in the special contracts sections, particularly in franchise<sup>12</sup>. To be fair, this lack of attention is inherited by more consolidated texts such as Unidroit principles and PECL, where references to contractual networks are also missing.

References to multilateral contracts, one form of contractual networks, are sporadic, despite the very real existence of consolidated models such as consortia and European Economic Interest Group (EEIG). Conceptually, contracts are still mainly viewed as systems of bilateral exchanges differentiated from organisational contracts, such as those creating companies, meant to include several parties, and generating a corporate organisation. The line between exchange and organisational contracts is not discrete<sup>13</sup>. Complex contractual exchanges, involving a plurality of enterprises, often located in territories with different legal regimes, require some degree of governance. These are generally long-term, relatively stable relationships which differ from pure market transactions<sup>14</sup>. They require a specific legal framework because acting in a different environment where the combination between competition and cooperation among contractual partners is different from that in pure market transactions<sup>15</sup>.

So far, contractual networks have not been adequately recognised at European level where, at least implicitly, the traditional partition between exchange and organisational contracts has held firm<sup>16</sup>. The Council asked the European Commission to define a new

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<sup>12</sup> See Study Group on European Civil Code, *Principles of European law - Commercial Agency, Franchise and distribution Contracts*, (Oxford: OUP, 2006) and then the complete *Principles, Definitions and model Rules of European private law*, Draft Common Frame of Reference (DCFR), (Muenchen: Sellier Law publishers, 2008). According to DCFR, 'a franchise network consists of a franchisor and the group of all franchisees that operate the same business method and the existing liaison among them'.

<sup>13</sup> See below text and footnotes.

<sup>14</sup> On the difference between market transactions and contractual governance see O. Williamson, 'The economics of governance', cit., 1. For a different perspectives see O. Hart and J. Moore, 'Contracts as reference points', available at <http://www.chicagogsb.edu/research/workshops/theoryoforg/docs/hart-contracts.pdf>.

<sup>15</sup> On the relationship between cooperation and competition in contracts see R.E. Scott, 'Conflict and Cooperation in Long-Term Contracts', 75 *Calif. L. Rev.*, (1987), p. 2005. In relation to the European context S. Deakin, C. Lane and F. Wilkinson, 'Law, trust and incentives to cooperation', in S. Deakin and J. Michie (eds), *Contracts, Competition and Cooperation*, (Oxford: OUP, 1997); G. Teubner, *Netzwerk als Vertragsverbund - Virtuelle Unternehmen, Franchising, just in time aus sozialwissenschaftlicher und juristischer Sicht*, (Oxford: Hart, 2004), and Id., 'Coincidentia oppositorum: Hybrid networks beyond contract and organisations', cit.

<sup>16</sup> See the Commission Communication to the European Parliament and the Council, *A more coherent European contract law – An Action Plan*, 12.02.2003, COM(2003) 68 final; the Commission Communication to the European Parliament and the Council, *European contract law and the revision*

framework for small and medium enterprises SMEs<sup>17</sup>. I The Commission launched a program to draft a Small Business Act which will include a company law statute for SMEs<sup>18</sup>. References to networks of SMEs are made in specific projects aimed at promoting innovation. They are mainly concerned with services provision to promote the creation of a single market<sup>19</sup>.

Despite this inattention both by European contract law drafters and by private international law, networks, especially those among SMEs, have gained momentum in policy-making. The ever more frequent references to networks, both contractual and organisational, in relation to policies associated with competitiveness and growth suggest that it may be necessary to coordinate with the governance dimension associated with their private law regimes<sup>20</sup>.

The increasing importance of networks at EU level forces us to rethink two main policy issues: 1) how, and according to which variables, it is important to define the divide between contract and company law in relation to inter-enterprise coordination; 2) how to regulate multilateral contracts among enterprises.

I suggest that the recognition of these contractual networks should imply their integration in the process of harmonisation of European contract law, currently in the DCFR, although their specificity may require the definition of a set of separate principles that must, thereafter, be coordinated with the general principles of contract law<sup>21</sup>. Even if only coordination were required, fundamental questions, concerning the

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*of the Acquis : the way forward*, 11.10.2004, COM(2004) 651 final, and also the DCFR, cit., where a contract is defined in Book II, art 1:101 as ‘*an agreement which gives rise to, or is intended to give rise to, a binding legal relationship or which has, or is intended to have, some other legal effect. It is a bilateral or multilateral juridical act*’.

<sup>17</sup> See Communication from the Commission, *A single market for 21<sup>st</sup> century Europe*, 20.11.2007, COM(2007) 724 final; Communication from the Commission, *Small and medium enterprises - Key for delivering more growth and jobs - A mid-term review of modern SME policy*, 4.10.2007, COM(2007) 592 final.

<sup>18</sup> References to a European private company statute were made in the parliament Resolution adopted on February 1<sup>st</sup>, 2007 where the Parliament has defined, mainly in the Annex, the most relevant features of the Statute. The Communication on Single market for 21<sup>st</sup> century has taken a broader approach referring to a Small Business Act which will certainly include the Statute but will go beyond: ‘*The Commission will examine a range of initiatives to back SMEs, in the form of a Small Business Act for Europe in 2008. This could provide guidelines and provisions tailored for SMEs according to the “think small first” principle*’.

<sup>19</sup> See Decision 1639/2006/EC of the European Parliament and of the Council of 24 October 2006, establishing a competitiveness and innovation framework programme (2007-2013), O.J. 9.11.2006, L310/15.

<sup>20</sup> See the Final Report of expert group on ‘Supporting the internationalisation of SMEs, European Commission, DG Enterprise and Industry, December 2007; the Final Report of expert group on ‘Enterprise clusters and networks’, European Commission, DG Enterprise, 2002; the Communication from the Commission to the Council, the European Parliament, the European economic and social committee and the Committee of the regions, ‘Small and medium-sized enterprises – Key for delivering more growth and jobs. A midterm review of Modern SME policy’, Brussels, 4.10.2007, COM(2007) 592 final; and the speech of G. Verheugen, ‘Small business act for Europe’, Commission hearing, Brussels, 6.02.2008, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/165&format=HTML&aged=0&language=EN&guiLanguage=en>.

<sup>21</sup> In the DCFR multilateral contracts are recognised among the legal relevant acts. However, the provisions concerning the general part of contract law in book II and III are all devoted to bilateral contracts. A different perspective emerges from special contracts.

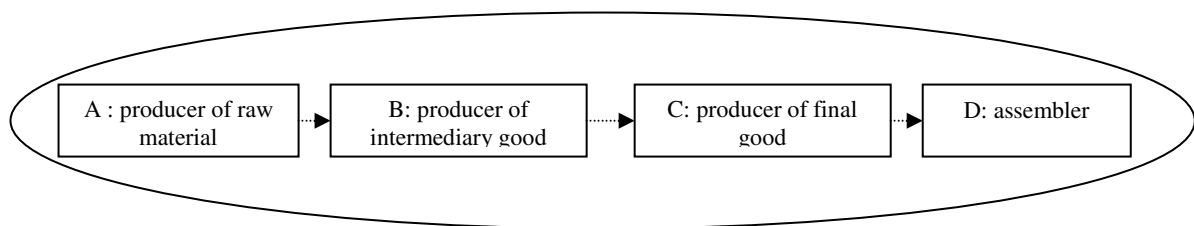
correlation between general contract law and contractual networks, have to be addressed both at EU level but also between EU and MSs. For example, the role of *privity* or its functional equivalents such as le *principe de relativité du contrat* in European contract law, the possibility to conclude multilateral contracts, their legal regimes as to validity, breach, individual and collective termination, admissibility of a governance structure, creation of separate legal entities to manage assets necessary to administer the network, etc.

The paper proceeds as follows: in part III the concept and application of contractual interdependence will be clarified, focusing on two of the existing models of contractual networks, namely the case of multilateral contracts and the case of ‘linked contracts’. In part IV, the need for harmonisation will be proved not only by reference to contract law’s reluctance to address issues concerning contractual networks, in particular in post-contractual phases. Part V presents a brief overview of the interplay with Private international law and the necessity to coordinate legal reforms at EU level. In part VI, some conclusions and a proposal for future development will be presented.

### III. Contractual Networks and the Traditional Partitioning between Contract and Company Law in Inter-firm Cooperation

The focus in this essay is on contractual interdependencies, i.e., how legal systems configure the coordination of relationships characterized by strong economic interdependency among enterprises<sup>22</sup>. Contractual networks can operate in the production phase, the distribution phase or can coordinate vertically arranged phases along the chain. When they operate within one phase they can be termed a horizontal network, whereas when they encompass multiple phases they may be described as vertical networks. Horizontal networks tend to be participated in mainly by competitors, and, consequently, they require a different combination of competition and cooperation rules to vertical networks<sup>23</sup>.

Table 1



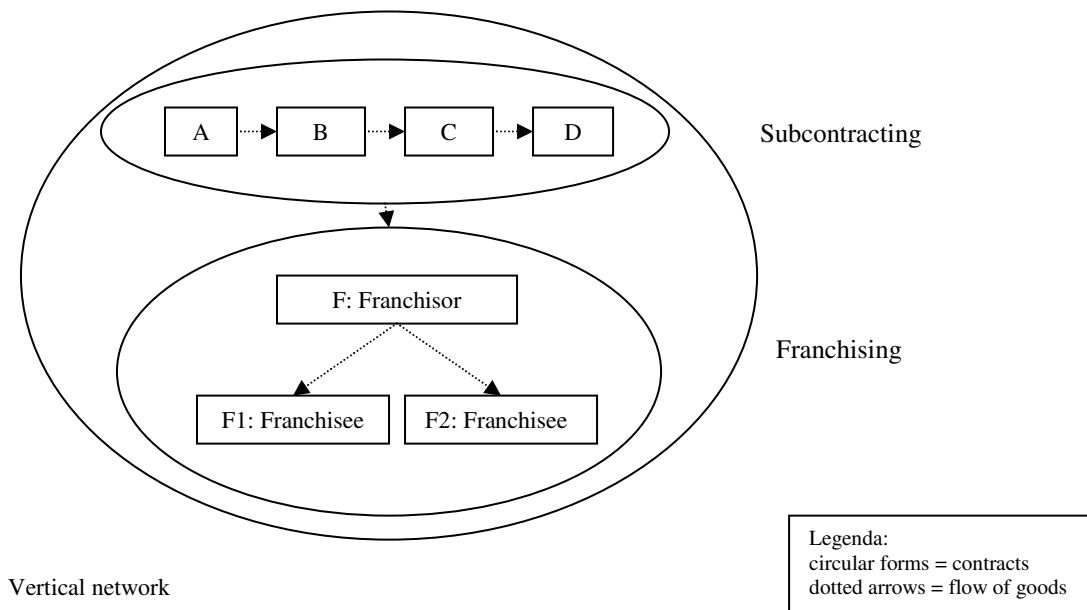
Horizontal network: consortium of enterprises along the supply chain.

Legenda:  
 circular forms = contracts  
 dotted arrows = flow of goods

<sup>22</sup> Such interdependency may give rise to contractual networks in addition to other legal forms of contractual coordination.

<sup>23</sup> B. Nooteboom, ‘Innovation and inter-firm linkages: new implications for policy’, *Research Policy*, 28, 1999, pp. 793-805; Id., *Inter-firm Collaboration, Learning and Networks: An Integrated Approach*, London, Routledge, 2004.

Table 2



The potential participants in the network may have homogeneous or at least partially divergent interests<sup>24</sup>. Moreover, the ‘collective interest’ of the network may differ from those of individual participants. These features may affect the formation of the network and its governance structure. Divergences can concern the form of the network; litigation may arise as to whether the network exists<sup>25</sup>, because some participants may wish to emphasize its existence and some may prefer fragmentation and separation, asserting its inexistence. More often, this disagreement may occur as to the shape of the network and its main scope.

One potential response to conflicting interests, giving rise to the disagreement, may be provided by general clauses<sup>26</sup>. In particular, the duty of loyalty plays a much stronger role than in bilateral exchange contracts<sup>27</sup>.

Networks may be partial, i.e., individual contracts may design common features concerning risk-allocation, risk-management and risk-sharing, whilst leaving full independence and autonomy in other matters<sup>28</sup>. Often the network is used efficiently to

<sup>24</sup> W. W. Powell, K. W. Koput and L. Smith-Doerr, ‘Interorganizational Collaboration and the Locus of Innovation: Networks of Learning in Biotechnology’, *Administrativ Science Quartely*, 1996, 41, 1, pp. 116-145; C. Menard, ‘The economics of hybrid organisations’, cit., p. 353.

<sup>25</sup> See Cass. civ., sez. III, 12.07.2005, n. 14611, where the contracting parties of two linked contracts claimed the existence or the inexistence of the link between a lease contract of a building and an agency contract, in order to confirm or deny the application of different rules on the lease.

<sup>26</sup> On the role of good faith in contractual networks, see F. Cafaggi, ‘The regulatory function of contract law’, unpublished manuscript on file with the author.

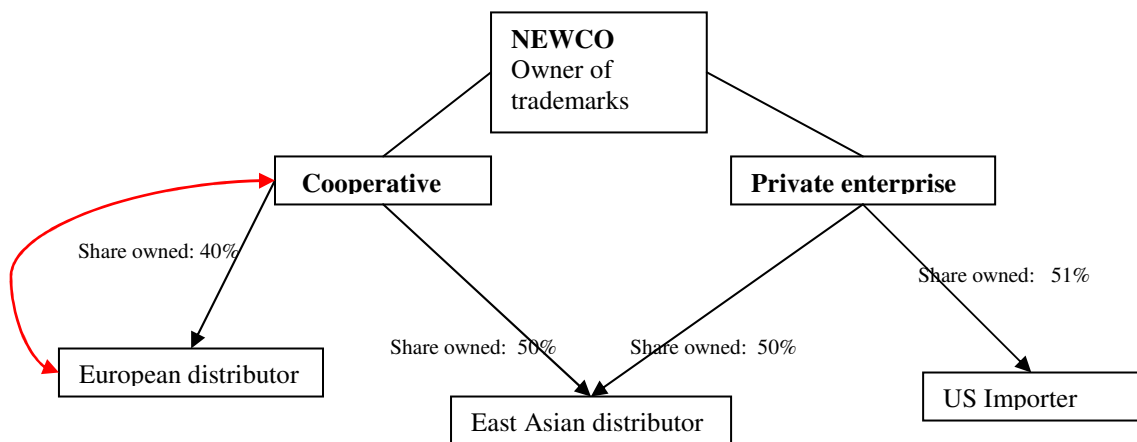
<sup>27</sup> See F. Cafaggi, ‘Organizational loyalties and models of firms: governance design and standard of duties’, in *Theoretical Inquiries in law*, 2005, 518 ff., where loyalty in hierarchical vertically integrated firms is compared with loyalty in networks.

<sup>28</sup> Typical examples are exclusion clauses or clauses that limit liability. For example, in a contract where the subcontractor (B) limits the liability to a certain ceiling in its relation to its main contractor (A), the subcontractor of the subcontractor (C) sued by A claims a defence based on the contract between A and

allocate liability along the supply or distribution chain, though contracts remain independent for other purposes. On the contrary, complete networks imply full coordination and a higher degree and intensity of interdependence<sup>29</sup>.

Contractual networks are generally problematic for traditional partitioning in legal systems because they are located at the intersection between exchange and organisational contracts, thus, in the conventional view, between contract and company law<sup>30</sup>. While one might easily recognise that no sharp divide exists between the two models, which are better characterised as *idealtypes* than real alternatives, it is often the case that locating a contract within the exchange or the organisational category still implies different legal consequences, in terms of liability within the ‘network’, but also towards third parties just to mention one single, yet relevant, issue. When contractual networks combine coordination and exchanges among participants, they display a higher level of complexity. In this case, they often encompass some form of governance and require administrative costs higher than ordinary bilateral exchange contracts<sup>31</sup>. This governance is often associated with monitoring and regulatory functions. They incorporate a higher level of regulatory functions concerning common rules that parties must use to define bilateral relationships within the network and, sometimes even more importantly, when the network enters into contractual relationships with third parties (i.e., the final producer with distributors, the distributor with consumers and so on).

Table 3



B. Similar examples may concern information production or transfer which are characterized by covenants of confidentiality or covenant not to compete encompassing covenants not to use the information produced by the network for individual profit.

<sup>29</sup> See R. Gulati and H. Singh, ‘The Architecture of Cooperation: Managing Coordination Costs and Appropriation Concerns in Strategic Alliances’, *Administrative Science Quarterly*, 1998, 43, 4, pp. 781-814. The degree of interdependency refers to the influence of decision making by one enterprise over the other, the intensity to the frequency of relationships among enterprises over time

<sup>30</sup> See V. Goldberg, ‘Toward an Expanded Theory of Contract’, *Journal of Economic Issues*, 1976, 10, pp. 45-61; O. E. Williamson, ‘The Economics of Governance’, *American Economic Review*, 2005, 95, 2, pp. 1-18; E. Schanze, ‘Symbiotic arrangements’, 149 *Journal of Institutional and theoretical economics*, 691 ff.

<sup>31</sup> See, for an example of such a complex structure, the model in Table 1

Monitoring the performance of individual parties is also a relevant function of the contractual network<sup>32</sup>. Contractual interdependency implies the necessity of collective monitoring of network members' performance to ensure that the final result will be achieved. This monitoring concerns individual performance, when for example quality and safety control implicates each phase along the supply chain, but it may also implicate attentiveness to market evolutions, enabling the network effectively to adapt to market changes. Coordination in monitoring may allow earlier error detection and correction<sup>33</sup>. Often complex contractual performances need adjustments over time that imply changes to be communicated among parties<sup>34</sup>. Hierarchical monitoring, typical of pyramidal groups is inappropriate. Contractual networks require different legal frameworks for effective monitoring. This monitoring may be regulated either by duties to cooperate and to behave loyally towards the other members, or through a more specific governance structure, such as committees or other organisational devices. Flexible responses to external events, i.e market changes in demand or supply, often characterize the comparative advantage of the network in relation to vertically integrated firms.

Before starting the analysis concerning the network forms, it is important to underline that contractual networks have a double dimension: one internal, concerning the relationships among their members, and one external, concerning the relationship with third parties. This distinction suggests the relevance of boundaries. How are the boundaries of the network drawn? What differences exist between third parties, members of the network, and third parties located outside the network? Should the regime concerning third party protection of network participants be differentiated from that of non-members? How can this distinction be clearly drawn? Answers to these questions, beyond the scope of this paper, should provide the guidelines for a specific legal regime concerning contractual networks<sup>35</sup>.

Contractual networks differ significantly from long-term bilateral contracts because the level and quality of interdependence is higher, often requiring a governance system<sup>36</sup>. This implies that different rules are needed for duties to cooperate, invalidity, remedies for breach, termination, and dissolution<sup>37</sup>.

Contractual networks also differ from companies because they do not constitute a separate legal entity. Thus, when they enter into contractual relationships with third parties they must use contractual arrangements, such as agency or mandate, to enable conclusion of contracts by a representative, acting on behalf of the network. This

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<sup>32</sup> See C. Sabel, *Learning by monitoring*, (Cambridge, MA: Harvard University Press, 2006); Id., 'A Real Time Revolution in Routines', C. Heckscher and P. Adler (eds), *The firm as a collaborative community*, (Oxford: OUP, 2006).

<sup>33</sup> See C. Sabel, *Learning by monitoring*, cit.

<sup>34</sup> See C. Sabel, 'A Real Time Revolution in Routines', cit.

<sup>35</sup> See F. Cafaggi, 'The multiple faces of contractual network', unpublished manuscript.

<sup>36</sup> See C. Menard, 'The economics of hybrid organisations', cit., p. 362.

<sup>37</sup> The Transaction Cost Economics doesn't pay so much attention to differences between long-term contracts and contractual networks as it considers only the single bilateral contract. Hence, it undervalues the governance matters coming from the links between several bilateral contracts. See O. E. Williamson, 'Comparative Economic Organization: The Analysis of Discrete Structural Alternatives', 36 *Administrative Science Quarterly* 269, 280 (1991). For a critic to this approach see W. W. Powell, 1990, cit., pp. 303-304.

‘external dimension’ is also related to asset-partitioning and creditors rights. The literature on asset-partitioning has showed quite clearly that there is a continuum between contracts and organisations, but differences in the two polar models are significant<sup>38</sup>. Generally, the members of the contractual network are fully liable for obligations undertaken by the network. Different devices for shielding their assets and separating them from that of the network can be used<sup>39</sup>.

In this paper, I will concentrate on the ‘internal’ dimension, focusing on the relationships among the members of the contractual network.

### **1. The Model of Contractual Interdependency and Modes of Implementation**

Contractual relationships in networks are often linked because there are interdependencies of contract formation and/or implementation. These interdependencies exist in contracts between enterprises and in those between enterprises and consumers<sup>40</sup>. However, not all contractual interdependencies amount to a network. The degree and forms of interdependency constitute the network’s form, although the divide between this and a traditional long term contract is more scalar than binary.

The network form is a specific type of interdependency that increases coordination among enterprises. What are the sources of such interdependency? Interdependency occurs when joint investment decisions have to be made, but also when parties want to protect a shared common good, such as reputation. Interdependency may also be associated with *intuitus personae*, as in contracts characterised by *uberimma fides*: the higher *intuitus personae* among contracting parties, the stronger the level of interdependency.

Networks can have a pro-active or re-active function. Thus, they can generate new goods or protect existing ones. For example, in consortia, where enterprises decide to produce one product or several products with the same trademark, a high level of interdependency is required. Parties need to define their level of cooperation, to regulate competition with other products manufactured individually, to define common quality

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<sup>38</sup> See H. Hansmann and R.H. Kraakman, ‘The essential role of organisational law’, NYU Law and economics Working papers, 6, 2000, available at [http://ssrn.com/abstract\\_id=229956](http://ssrn.com/abstract_id=229956); H. Hansmann, R.H. Kraakman and R. Squire, ‘Law and the rise of the firm’, ECGI Working papers, 57, 2006, available at [http://ssrn.com/abstract\\_id=873507](http://ssrn.com/abstract_id=873507); E. Iacobucci and G. Triantis, ‘Economic and legal boundaries of firms’, Virginia Law review, 2007, available at [http://ssrn.com/abstract\\_id=903328](http://ssrn.com/abstract_id=903328).

<sup>39</sup> For a general overview H. Hansmann and R.H. Kraakman, ‘The essential role of organisational law’, cit.; E. Iacobucci and G. Triantis, ‘Economic and legal boundaries of firms’, cit.

<sup>40</sup> Typically interdependences in consumer contracts are those which associate sales and financing contracts or sales and service providing contracts, typically in the software sale domain. A specific reference to interdependency can be found in directive n. 93/13 concerning the criteria to interpret unfair terms by reference to other contracts. See for national implementation loi 95-96 du 01/02/1995 concernant les clauses abusives et la présentation des contrats et régissant diverses activités d'ordre économique et commercial, J.O. 02/02/1995, 1755 ; Unfair terms in Consumer Contracts Regulations 1999. Statutory instruments, 22/07/1999, n° 2083 ; Gesetz zu Regelung des Rechts der Allgemeinen Geschäftsbedingungen (AGB-Gesetz) vom 09/12/1976 (BGBl. I 1976, 3317), zuletzt geändert durch Gesetz vom 19/07/1996, Bundesgesetzblatt Teil I, 1013; Legge 3 febbraio 2003, n. 14 - Disposizioni per l'adempimento di obblighi derivanti dall'appartenenza dell'Italia alle Comunità europee, GURI, 31 del 07/02/2003.



control systems, rules that would ensure obligations to cure defects if products do not comply with agreed standards, and remedies to ensure that the goals of the network cannot be undermined by individual breaches.

A different example is that of franchise or other distribution contracts. Here, whereas the trademark is generally owned by the franchisor, the reputation of the network may increase or decrease franchisees' incentives to make specific investments. A legal regime that conceives of distribution and franchise contracts as a set of purely bilateral contracts could fail to capture these interdependencies and provide a sub-optimal legal framework, because in this case it discourages investments by detracting from their efficiency<sup>41</sup>.

While the network form can be characterized by a significant level of stability, the legal regime is aimed at striking a balance between stability and flexibility, in particular concerning entry (the right to join the network) and exit (the right to cede) from the network. Network contracts often emerge as a response to uncertainty, displaying comparative advantages in respect to bilateral exchange contracts. They may allow better management both of *ex ante* uncertainty, when parties are not informed about the nature of performance and need to define the content, its quality and quantity during the relationship, and *ex post* uncertainty, where parties have to renegotiate. But uncertainty may also concern the width of the network<sup>42</sup>. Networks can also result in better tools to address exogenous shocks, determined by market variations, to permit more efficient ascertainment of the best insurer for unanticipated losses. This advantage is often associated with an appropriate contract design.

Interdependence often increases the risk of opportunism<sup>43</sup>. As it is the case for bilateral contracts also contractual networks call for specific responses to opportunism and free riding. Appropriate institutional design requires specific criteria to evaluate performance and breach and the consequences of individual exit when resources and capabilities are shared.

Contractual networks may be harder to interpret within the *ex ante/ex post* divide which has characterized most of the recent contract literature concerning the use of standards

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<sup>41</sup> See M. Hesselink et al., *Commercial agency, franchise and distribution contracts*, (Munich: Sellier European Law Publisher, 2006).

<sup>42</sup> The width of the network might be unknown to the initial parties and thus the ability of the parties to define clauses that should be inserted in all contracts related to the network to ensure coordination due to economic or technological interdependence might be limited. For example, A, contractor, can ask B to supply a certain quantity of goods, but it is unknown how many enterprises will be involved in that production process, this is also due to recent regulatory changes that have multiplied obligations to perform quality control. When A and B conclude the contract they do not know the number of enterprises involved, thus they may not be able to plan in advance clauses that should be inserted in the subcontracts to ensure the achievement of the targets. The network will grow over time and coordination issues will arise. In this case, the link might be established by judicial interpretation as well.

In the context of distribution contracts, distributor might not know exactly which products are needed and be willing to choose different parties thus determining the structure of each contract at different time. In this case the distributor contracts with the network of suppliers and will arrange bilateral linked contracts depending on market evolution.

<sup>43</sup> See C. Menard, 'The economic of hybrid organisations', cit. p. 355.

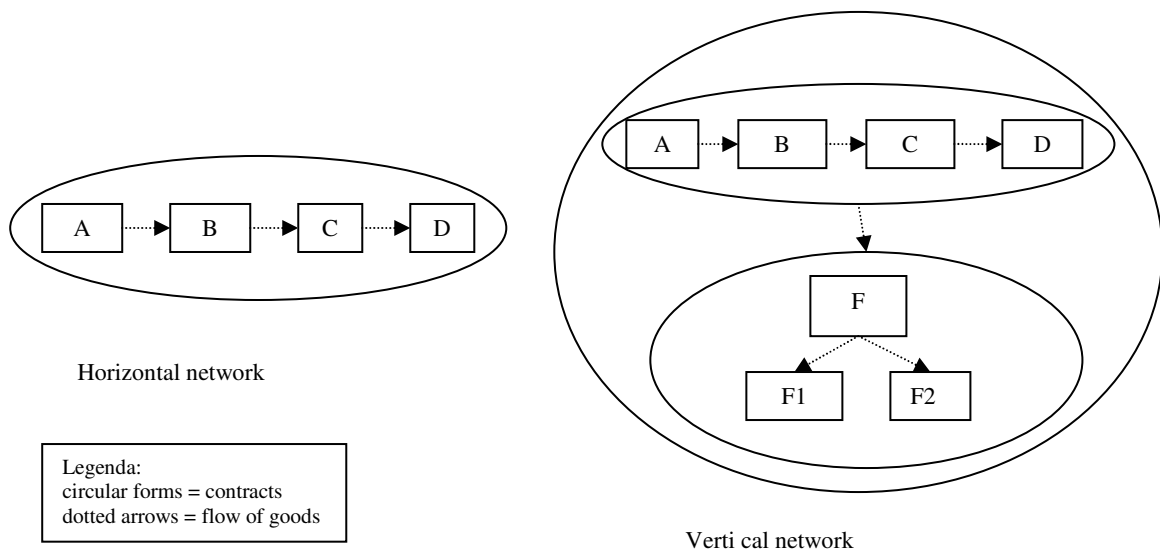
and rules<sup>44</sup>. Borrowing from organisational literature, they can be better characterized as organisational co-makerships, where enterprises co-design contracts by reacting to contingencies and redefining the terms of the contract to match the evolution of the relationship in response to endogenous (for example increase or decrease of trust) and exogenous factors (for example increase of competitive pressures, increase or decrease of input factors, etc.)<sup>45</sup>.

## 2. *The Forms of Contractual Networks*

Contractual networks can take at least four different legal forms<sup>46</sup>.

A) A multilateral contract, where three or more parties agree to coordinate complex economic operations such as part or whole production, the distribution chain or both. A typical example is the contract of consortium.

Table 4



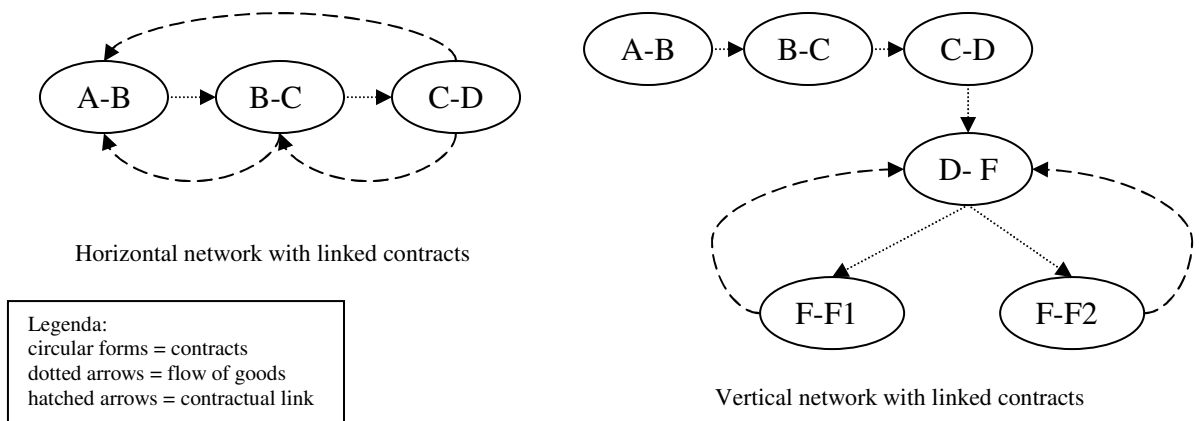
<sup>44</sup> See R. Scott and G. Triantis, 'Anticipating litigation in contract design', *Yale Law Journal*, 2006, 115, 814.

<sup>45</sup> See C. Sabel, 'A Real Time Revolution in Routines', cit. There is a debate in social science concerning the function of contracts in networks. Some believe that it should only provide the framework for parties to cooperate, some believe that it should facilitate adaptation by parties to unanticipated circumstances. B. Klein, 'Vertical integration as organisational ownership: the Fisher Body-general motors relationship revisited', cit., p. 199; Id., 'Why Hold-Ups Occur: The Self-Enforcing Range of Contractual Relationships', *Economic Inquiry*, 1996, 34, 3, pp. 444-463; O. Williamson, 'The economics of governance', cit.; M. Gravenotter, 'The strength of weak ties', in *American journal of sociology*, 87, p. 1360; R. E. Scott, 'Conflict and Cooperation in Long-Term Contracts', *California Law Review*, 1987, 75, 6, pp. 2005-2054.

<sup>46</sup> The number of structural forms can be infinite. The effort is to distinguish different forms of contractual network according to the current conceptual devices existing in most legal systems.

B) Set of interdependent “linked” bilateral contracts. Examples in the supply chain might be subcontracting; examples in the distribution chain might be distribution contracts, franchise, licensing, etc.<sup>47</sup>

Table 5



C) An intermediate form consists in a multilateral contract as a framework contract and bilateral executory contracts between parties to regulate the specific elements of the transaction<sup>48</sup>. Unlike model A (pure multilateral contract), this contractual design

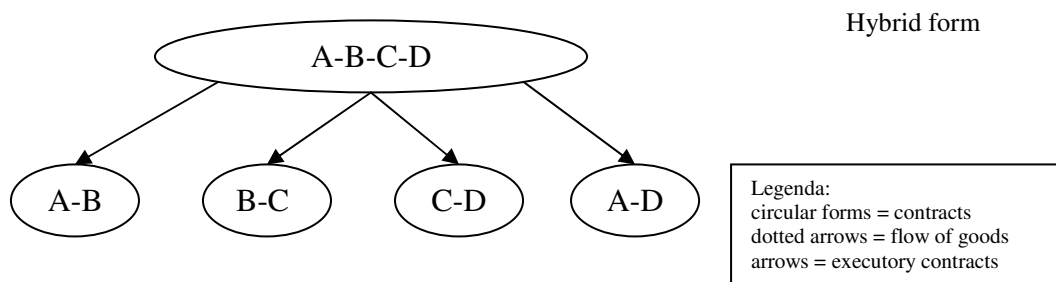
<sup>47</sup> For example, in case of vertical networks the link among the contracts could make available for the franchisee (F1 or F2) an ‘action direct’ towards the producer of the goods (D), if the consumer claim the existence of defects or malfunctioning of the goods.

<sup>48</sup> This model is well identified in the case law of some legal systems. For example in Italy see Tribunale Torino 3 febbraio 1993, *Giur. It.* 1994, 581 ff.

German Law does not restrict the enforceability of multilateral framework contracts. For instance, construction contracts are often linked together in this way. See, for instance Börner, ‘Netzwerke komplexer Langzeitverträge: Möglichkeiten des multilateralen Interessenausgleichs’, in Nicklisch (ed.), *Netzwerke komplexer Langzeitverträge* (2000), p. 53, 65; more specifically Schwarze, *Das Kooperationsprinzip des Bauvertragsrechts* (2003), p. 189.

French scholars, more than French courts, have developed the category of the “*contrat cadre*”, as the contract which establishes the rules according to which future contracts (the so called *contrats d’application*) will be entered into in order to fulfil the goals fixed in the “contract cadre” (See, Pallaud-Dulian and Ronzano, ‘*Le contrat-cadre, par delà les paradoxes*’, in *Revue trimestrielle de droit commercial et de droit économique*, 1996, 179. See footnote n. 103). The Avant-Projet de Réforme contains a provision (Art. 1102-6) defining the *contrat cadre*, without establishing peculiar and specific legal effects for these contracts, in terms of validity, performance, etc. Nevertheless, according to the official comment (p. 25), Art. 1121-4 (objet) ought to be interpreted in connection with the phenomenon of *contrats-cadre*. On the contrary, French scholars have not, so far, deepened the issue concerning the plausibility of a *contrat cadre* with more than two parties (multilateral contrat): nevertheless, apparently, there are no obstacles (in the French legal system) to such a legal scheme.

permits more flexibility because it allocates only the common features to the framework contract and leaves individual parties freedom to negotiate the other elements<sup>49</sup>. On the other hand, it differs from model B because it provides for a higher level of coordination through the framework contract. Technically, it also helps solving problems associated with privity or its functional equivalents, given that in this case parties of bilateral contracts undertake obligations under the framework contract which allow them to bring legal claims even if they are not parties to the same executory contract. However, the extent to which multilateral framework contracts are directly enforceable and give rise to legal claims varies in different MSs<sup>50</sup>.



Another interesting distinction to be considered is that between "*contrat-échange*" et "*contrat-organisation*", as suggested by P. Didier (in *L'avenir du droit, Brèves notes sur le contrat-organisation* Mélanges Fr. Terré, Dalloz, PUF, Éd. Juris-Classeur, 1999, p. 635-642), who considers the "contrat de société" as a typical example of *contrat-organisation*, i.e. a contract whose object is not simply the sale of goods or services, but, rather, the creation and regulation of an organization, a mechanism through which taking decisions for future legal acts, suitable to improve the original contract. The *contrat-organisation*, like its paradigm (archetype), i.e. the *contrat de société*, could certainly be multilateral. With regard to the English legal system, the concept of framework contract is often adopted by British judges in their rulings, in order to indicate a contract providing the terms on which future acts (contracts) will be entered into (see *Lettings International Limited v. London Borough of Newham*, Case No: A2/2007/2841, [2007] EWCA Civ 1522). A recent paper investigates the multiple issues connected with the so called "umbrella agreements", defined as "*private arrangements that provide a framework of clauses which regulate future contracts*": "*they explicitly spell out the principles that guide future contractual decisions*" (S. Mouzas, M. Furmston, *From contract to umbrella agreement*, in *Cambridge Law Journal*, 2008).

<sup>49</sup> This model differs from the complex contract which is a contract incorporating different contracts. In this model bilateral contracts are independent and the function of the framework contract is that of identifying only the common features. On the distinction between complex contracts and linked contracts see for the Italian legal system, see Cass. 28.06.2001, n. 8844.

In the German law system, the concept of the framework contract ("*Rahmenvertrag*") is understood as a contract that only defines general points, but requires additional contracts which define the details on a case by case basis (for a definition, see, for instance: *Münchener Kommentar zum BGB-Kramer, Introduction Schuldrecht Allgemeiner Teil* (Vol. 2 a), para. 98). While 'linked contracts' are a different concept, defining two individual (self-contained) contracts which are economically linked together. See the definition (focussing mainly on sales contracts and linked loan agreements) in art. 358 para. 3 of the BGB. However, the German system does not acknowledge as a technical category the 'complex contracts', even though the term is sometimes used to describe contracts that are more complex than simple spot contracts (in any sense, i.e. because they are multilateral ['*komplexe Netzverträge*'], long-term ['*komplexe Langzeitverträge*'] or due to their content).

<sup>50</sup> On the bindingness of framework contract and normative contracts, in case of executory contracts, see A. Orestano, *Accordo normativo e autonomia negoziale*, (Padova: Cedam, 2000); G. Gitti, *Contratti regolamentari e normativi*, (Padova: Cedam, 1994).

The framework contract is signed by A, B, C, D, E, and F; it may contain obligations concerning the allocation of risks and liabilities, norms of contract interpretation, remedies, in particular termination rights. Adjacent to this, A and B, C and D, E and F, conclude separate contracts. The intensity and specificity of the framework contracts content may vary depending on the level of ex ante uncertainty and the need for flexibility that individual contracting parties want to enjoy.

If A breaches the contract concluded with B, the other participants to the framework contract, - C, D, E, and F - can bring a legal claim for breaches of obligations undertaken in the framework contracts.

A different set of problems concerns situations where one party is affected by the breach of a contract concluded by two other parties<sup>51</sup>.

D) Contracts for the benefit of a third party. The fourth model is based on a series of interrelated contracts for a third party beneficiary. Here, the peculiar feature is that there are multiple beneficiaries.<sup>52</sup>

The network is composed of five enterprises A, B, C, D, E. A and B conclude a contract for the benefit of C, D, E; while B and C conclude a contract for the benefit of A, E, B, and so on. There will be four contracts for the benefit of the five participants to the network.

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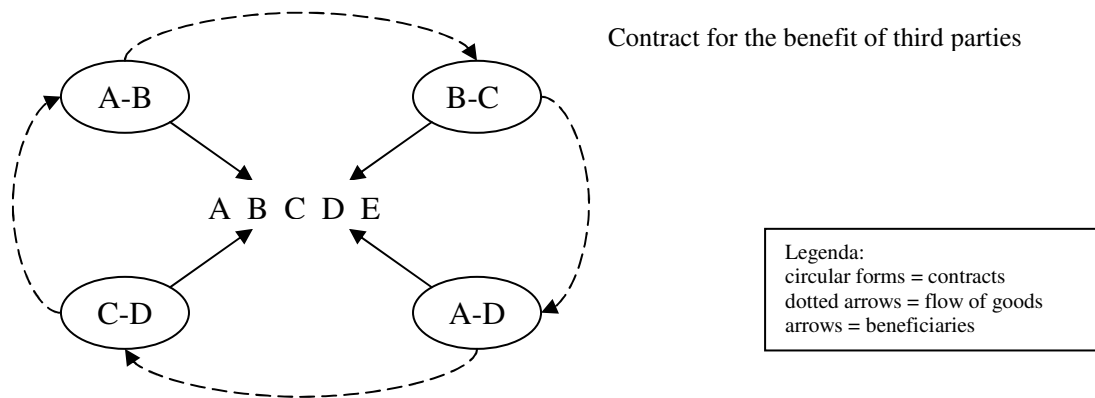
<sup>51</sup> For example, A and B conclude a contract limiting liability of B to 100. B and C conclude a contract, limiting C's liability to 200. C is in breach, B is insolvent and A sues C to recover losses that should have recovered from B had it not been insolvent.

<sup>52</sup> On a comparative perspective, see G. Gandolfi, 'Il contratto a favore di terzi nel "Codice Europeo dei contratti"', Riv. trim. dir. proc. civ., 2003, p. 993; L. Vagni, 'Il contratto a favore di terzi nella comparazione "common law-civil law": dallo jus commune al diritto privato europeo', Riv. trim. dir. proc. civ., 2005, p. 1195.

In German law system, even though there are no references confirming explicitly, there is nothing which excludes the possibility to have multiple beneficiaries in a contract in favour of third party. However, the problem is rather that the legal positions of these multiple beneficiaries must be well-defined (Does everyone have an individual right to claim or can they only act on a collective basis? If so, is everybody granted the benefit on a pro-rata-basis or not?). These problems do not differ, however, from 'normal' contracts where with multiple beneficiaries (i.e. not third parties). See art. 428 BGB on this general issue.

In France, although the civil code (Art. 1121) and the more recent Avant-Projet Catala (Art. 1171 seq.) refers to the hypothesis of a contract in favour of a third party, "*stipulations pour autrui*" with several beneficiaries are admitted by Courts (see, Cass. Assemblée Plénière, 12 décembre 1986, n. pourvoi 84-17867, deciding on a life insurance contract, whose beneficiaries were the insured's children. The case is reported by Larroumet, *Les obligations, le contrat*, Paris, 2003, p. 970. An interesting research about the "*stipulations pour autrui*" and the life insurance contracts has been carried out by Kullman Jerome, *Stipulation pour autrui*, in *Revue Générale du Droit des Assurances*, 1998, p. 786 seq.; see, also, Cass., Comm., 23 novembre 1999, n. 96-16257). In the British system, the first case which applies the Contracts Right of Third Parties Act (1999), by enabling the third party to sue so as to obtain the performance, concerned a contract with two beneficiaries (See, *Nisshin Shipping Co Ltd v. Cleaves & Company Ltd and Others*, [2003] EWHC 2602 (Comm), Par. 13 seq. The action was brought only by one of the two identified beneficiaries).

Table 6



In this contribution, I will only address and compare the first two models<sup>53</sup>. However, it is important to recognise that, often, different general principles apply and thus the issue of interdependence is related to the width and the exceptions of the principle of privity and that of *relativité du contrat*<sup>54</sup>.

Particular level of complexity arises when, instead of domestic networks, trans-national European or intercontinental networks are in place. In this context, the legal regime may be determined by the law that parties choose for their contracts when they conclude them. Parties can define the applicable law and, lacking specific indications by the parties, private international law will apply.

Given that these principles vary in different MSs, the creation of a trans-national European network of SMEs presents highly complex problems when it is regulated by private international law, given, in addition, the structure and scope of article 4 of the Rome convention and Regulation Rome I, as it currently stands.

*a) The multilateral contract model*

Multilateral contracts are those where three or more parties agree to do, or to restrain from doing something. They may or may not involve property transfers. In multilateral contracts, unlike bilateral contracts, there are more than two parties and each one undertakes obligations towards each party of the contract in order to achieve a common goal. Unlike companies or other legal entities, where the obligations are owed towards

<sup>53</sup> See for an illustration of the third and the fourth model, F. Cafaggi, *Complex contractual networks*, unpublished manuscript on file with the author

<sup>54</sup> The foundations of privity are certainly different from those of *relativité de contrats*. The link between the doctrine of privity and that of consideration is widely explored in the English literature. This link has however been limited by the House of Lords in *Scruttons Ltd. V. Midland Silicones* [1962] AC 446, and *Beswick v. Beswick* (1966) Ch. 538, [1968] AC 58.

On the principle of *relativité du contrats* in French law, see A. Weill, *Le principe de la relativité des conventions en droit français*, (th. Strasbourg, Dalloz, 1938); J. L. Goutal, *Essai sur le principe de l'effet relatif du contrat*, (th. Paris, LGDJ, 1981). In Italian law, see M. Franzoni, 'Degli effetti del contratto', in P. Schlesinger, *Commentario del codice civile*, sub artt 1372-1373, (Utet: Milano, 1998).

the newly created entity and to the members, multilateral contracts generally do not imply the creation of an independent legal entity and are characterized by full liability of each participant. This model of contractual network often implies some degree of jointly made decision investments and resource pooling.

Notwithstanding the common features of the model, in practice, different types of legal structures have been developed. Whereas, on the one hand, there are purely contractual cooperation vehicles, which do not give rise to a proper organisation<sup>55</sup>; on the other hand, there are more structured forms of cooperation which present organisational characteristics<sup>56</sup>. In this case, generally, the vehicle created has power of negotiation and representation of its members and limitations of liability could be allowed to the same or similar extent as in the case of bilateral exchange contracts<sup>57</sup>.

It is important to specify that not all multilateral contracts constitute a contractual network. In order to have a network, the relationships among the parties should be characterized by a certain degree of stability (unlike those relationships which dissolve

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<sup>55</sup> This is the case of contractual (or unincorporated) joint ventures. Even if the joint venture has no precise legal definition, it can be described as a collaboration agreement whereby two or more enterprises, keeping their legal independence, agree to cooperate on an industrial or commercial project, simply organizing their cooperation on a contractual basis, through the coordinated exercise of each partner's enterprise, the synergistic use of resources brought by individual participants, a fair distribution of risks linked to the investment and sharing in the profits attained. Contractual joint venture is one of the two basic types of joint venture; the other one is the incorporated joint venture, in which parties create a new legal entity, organized as a corporation. Unlike incorporated joint venture, the contractual joint venture is generally characterized by two features: greater flexibility and greater exposure of the parties to liability. Usually, in fact, contractual joint venturers have joint and several liability.

In the international commercial law, also the consortium agreement could be seen as a collaboration agreement on a pure contractual basis and with no independent legal capacity. The consortium agreement as a temporary collaboration of parties, formed relating to a specific project, is often used in the construction sector in order to jointly prepare and submit to the customer a tender for a project and thereafter to execute the work. Another example of this is a common R&D consortium.

<sup>56</sup> See the rules on consortium in the Italian law whereby, according to the Italian civil code definition, more entrepreneurs create a common organization in order to regulate or to coordinate and perform one or more phases of their activity (art. 2602 c.c.); and the European Economic Interest Grouping (EEIG), introduced by Council Regulation 2137/85 of 25 July 1985 as an instrument for trans-national, cross-border cooperation between business entities operating within the EU. The purpose of the EEIG is 'to facilitate or develop the economic activities of its members and to improve or increase the results of those activities; its purpose is not to make profits for itself. Its activity shall be related to the economic activities of its members and must not be more than ancillary to those activities', *ibid* art 3(1). So far the grouping differs from a firm or a company. Nevertheless, the EEIG shall have full legal capacity, while the recognition of legal personality is left to the discretion of national legislation (art 1(3)).

Another example, in the international trade law, is the international consortium, defined as 'an organisation which is created when two or more companies co-operate so as to act as a single entity for a specific and limited purpose' (C. Murray, G. Dixon, D. Timson-Hunt and D. Holloway, *Schmitthoff's Export Trade. The law and Practice of International Trade* (London: Sweet & Maxwell, 2007), 343). In case of specific, large-scale construction or engineering projects, international consortia may take the legal form of an incorporated joint venture company or partnership.

<sup>57</sup> For example, the members of a consortium, as far as Italian law is concerned, have limited liability with respect to the obligations (and consequent debts) entered into by the consortium in its own name. For these debts, only the consortium is liable with the consortium fund, made of the contributions of the participants. On the contrary, according to the Council Regulation on the EEIG, while the grouping has principal liability for its debts, being a legal body separate from its members, nevertheless all the members of the EEIG have unlimited joint liability for these debts (see art 24).

once the economic operation for which they have been set up has been concluded) and by complementarity and interdependence, also concerning the strategic decisions that will affect the network as a whole.

The contractual network exists only if different parties coordinate economic activities performed by each participant. Multilateral contracts can coordinate enterprises within the same phase, production or distribution, or between two or more phases, in order to share complementary resources or risks. At the same time, unlike a company in the context of company law, each party retains its legal and economic autonomy. These tools can be implemented by companies or firms of any size, ranging from SMEs to multinationals, and also by other legal bodies governed by public or private law. In some cases, natural persons carrying on an industrial, commercial or other economic activity or providing professionals or other services can partake of these contracts<sup>58</sup>. Multilateral contracts can be used in order to combine some individual resources for a common undertaking, or to perform an ancillary role in respect to the economic activities of the individual participants, relating to their activities without substituting them<sup>59</sup>. They can be applied in a wide range of sectors: to develop joint research and development activities (usually requiring a high level of investments and complementary skills), for joint purchasing purposes and to develop a joint marketing strategy, to form a united front in the negotiation of raw material procurement conditions.

In this section I would like to describe very briefly five elements of the model to be contrasted with the linked contract model to be examined later:

- A. Systems of individual entry and exit of network participants (withdrawal, exclusion)
- B. Existence of governance structure
- C. Decision-making procedure
- D. Liability
  - 1. of the members towards the other members;
  - 2. of the members towards the collectivity/organisations;
  - 3. of the organisations towards the members.
- E. Termination/ Dissolution of the contract.

A. Multilateral contracts are often characterized by a flexible structure which permits the admission of new parties to the contract, without requiring any modification of the original agreement. The members are free to decide the requirements with which the new parties must comply to enter into the contract<sup>60</sup>.

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<sup>58</sup> Cfr. the EEIG, art. 4(1), b) Council Regulation n. 2137/85

<sup>59</sup> This is the case of the EEIG, in art 3(1), b) of the Council Regulation n. 2137/85.

<sup>60</sup> See art 26(1) Council Regulation n. 2137/85; art 16(1) (New Parties) of the ITC Contractual Joint Venture model agreement. See that the ITC Contractual Joint Venture model agreement is a model published by the International Trade Center, to which UNCTAD and WTO take part. It is specifically targeted at SMEs and designed for medium- or long-term cooperation as opposed to short-term or single-activity operations. There are two separate model agreement for contractual joint venture, one for two parties joint venture, and another for joint venture concluded by three or more parties. The main differences in the two-party contractual joint venture contracts concern the organization and management which are simpler, and the exit mechanism which is only an individual mechanism, and



Frequently unanimity is required to admit new members. Unanimous authorisation may also be the rule for the withdrawal of a member, in the absence of just and proper ground, or if different specific conditions are not laid down in the contract.

A typical cause for exclusion is the failure to fulfil obligations by a member. It should be noted that, usually, when a party fails properly to perform his obligations, the remedy for the breach of the contract made available in this model is the exclusion of the member, instead of the termination of the entire contract (as in case of bilateral contracts). As matter of fact, the multilateral contract aims to achieve a common goal, which can be still pursued, notwithstanding the breach of one member<sup>61</sup>.

Unlike companies with share capital, the multilateral contract model tends to accord greater importance to *intuitus personae*, and this is highlighted in the provisions regarding the admission and withdrawal of members and, more generally, in all the decisions involving changes in the composition of the contract (which require the unanimity rule).

B. Multilateral contracts may or may not give rise to an organisational body entrusted with coordination and monitoring power. This can occur through delegation to one participant or a third independent party. Monitoring performance can have different functions: in highly complex task it contributes to detect and correct errors<sup>62</sup>. It can also prevent opportunism from occurring or it provides early warning given the effects that breach can have on all the other participants as it is the case in strategic alliances, collective trademarks or consortia<sup>63</sup>. Information becomes a strategic resource in these type of networks. Traditional duties to inform are necessary but insufficient devices and often some type of governance body is required especially in transnational networks where physical proximity is missing. ICT have provided new platforms for extended contractual networks.

Considerable freedom is enjoyed by the parties to regulate multilateral contracts, as contract law provides only a general framework for the legal structure. Members are also free to decide upon the internal organisation and the voting procedures (except for fundamental decisions where unanimity is required).

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the existence of a the right to terminate the contract (instead of withdrawal and expulsion). In the latter model great importance is given to the common goal of the parties and to the opportunity of safeguarding the alliance created among the parties.

As to the consortium, Italian law gives leeway to the parties to define the admission requirements and procedure, only requiring a unanimity voting for decisions that involve changes in the contract (art 2607 c.c.).

<sup>61</sup> Italian law provides a general rule concerning the termination in case of non-performance: the multilateral contract can only be terminated if the breach is material for the all contracts. See, in the Italian legal system, arts 1455 and 1459 c.c., respectively on the gravity of the beach and the resolution of multilateral contracts, and arts 1463 and 1466 c.c. respectively on the impossibility to comply and impossibility in multilateral contracts. See also G. Villa, 'Danno e risoluzione contrattuale', in V. Roppo (ed.), *Trattato dei contratti – Rimedi 2*, vol. V, p. 751 ff.

<sup>62</sup> See S. Helper, J.P. MacDuffie, C.M. Sabel, 'Pragmatic collaboration: advancing knowledge while controlling opportunism', in *Industrial and corporate change*, 9, p. 471.

<sup>63</sup> See R. Gulati and H. Singh, 'The architecture of cooperation: managing coordination costs and appropriation concerns in strategic aloiances', in *Administrative science quarterly*, 43, p. 781 ff., suggesting that task decomposition is a major factor in governance design.

Sometimes a new entity is created. This can take the form either of a management body (for more structured multilateral contracts) or of a leading enterprise, acting as an agent, entrusted by a collective delegation made by all the members. Such entity would be responsible for the day-to-day management of the contractual activity. It implements decisions taken by the members and acts on behalf of the collectivity/organization when dealing with third parties<sup>64</sup>. The governance structure reflects, on the one hand, the fundamental role played by the members and, on the other hand, the opportunity to develop a governance mechanism for the unification/collection of the multiple members' wills, particularly when dealing with third parties. Members acting collectively usually opt for majority rule<sup>65</sup>.

C. Decisions are taken by members acting collectively. Members are free to choose methods and forms of consultation, adapting them to their particular requirements, and they could also choose the voting rights system, usually between voting rights proportionate to the owned shares or the alternative of granting each party one vote.

The rule of unanimity is the general rule of this model, unless the contract provides otherwise; however, being it very restrictive, it is usually kept for the most important decisions (e.g., decisions producing a change of the contractual rights or duties of the parties, or altering the object of the contract), while for all the other issues, a majority decision might be contemplated. Typically, unanimity is required to decide the winding up of the contract<sup>66</sup>.

D.1. and D.2. Each party is liable towards the collectivity/organisation and towards the other parties for obligations undertaken in the multilateral contract, which usually concern the behaviour, and the activity each member shall perform in order to pursue the aim of the contract and the duties to confer financial and non financial resources for the achievement of the common goal (initial and additional). In case of non-performance of party's obligations, the contract usually prescribes some sanctions (e.g., suspension of some right) against the party, in order to avoid the termination of the contract and to keep the commitment among the parties. The party failing to perform its obligation is held liable towards the other parties for losses and damages resulting from the breach.<sup>67</sup>

D.3. Members of the management body or the leading enterprise are liable towards the other members, according to agency rules, for the acts carried out, not falling within the objects of the contract<sup>68</sup>. Usually the contract provides also the conditions for the removal of the managers.

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<sup>64</sup> See art 19 and art 20 of the Council Regulation n. 2137/85; art 8 (Management Committee) of the ITC Contractual Joint Venture model agreement. For consortia in Italian law see artt 2606, 2608, 2612, c. 2, n. 4), c.c.

<sup>65</sup> See art 16 Council Regulation n. 2137/85; art 6 (Organization and management) and art 7 (Meeting of the parties) of the ITC Contractual Joint Venture model agreement; for consortia in Italian law see artt 2606, 2608 c.c.

<sup>66</sup> See art 31(1) Council Regulation n. 2137/85; art 25 of the ITC Contractual Joint Venture model agreement; for the consortia in Italian law see art 2607 c.c.

<sup>67</sup> See art 4 of the ITC Contractual Joint Venture model agreement; and art 13 Council Regulation n. 2137/85. For the consortia in Italian law see art 2603, c. 1, n. 1) e 7) c.c.

<sup>68</sup> Cfr. for the Italian legal system, arts 1703, 1705 and 1708 c.c.

E. The termination of the contract, but for material breach and impossibility, is generally decided by members by a unanimous decision.

b) *The 'Linked Contracts' Models*

This model is based on several bilateral, but in theory also multilateral, contracts, linked either via voluntary agreements or by the law, via judicial construction or statutory provisions. Contractual links may thus depend either on parties' will or on the structural features of the set of transactions<sup>69</sup>. A contractual network exists where there are two or more linked contracts among three or more contracting parties (heterogeneity) Several linked contracts between the same two parties (homogeneity) do not constitute a contractual network, rather a chain in my perspective.

Contracts in a network may be linked in different ways and for limited purposes: their validity or coming into force may be made conditional upon other contracts, the setting of prices may be made dependent on other contracts, the nature of the breach (material or otherwise) may be correlated with the interests of third parties, the selection of the appropriate remedy (damages versus specific performance) may be related to other contracts' performance or non-performance. The use of conditions is frequently used to link different contracts. The interdependence of these contracts may suggest the identification of complex synallagmatic relations, avoiding the partitioning of individual contracts<sup>70</sup>.

The recognition of such links may bring about different results. In certain contexts the invalidity of one contract will affect the validity of others, leading to an '*anéantissement en cascade*'; in other situations, a contract, considered invalid in a purely bilateral context, will be considered valid in the framework of a network<sup>71</sup>. Symmetrically a breach, though material in a bilateral context, may not be material in a network setting, where opportunities for substitute performance may be more numerous than those provided by a pure market context.

The linked contracts model of network is located between the single complex contract and separate bilateral contracts which may be instrumentally related but do not represent a unitary structure, without amounting to a contractual network<sup>72</sup>. Often the boundaries are not very clear cut. On the one hand, the definition of what is a single complex contract, in particular a multilateral contract where several parties concur, is not always

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<sup>69</sup> In France, scholars usually distinguish between "*indivisibilité objective*" and "*indivisibilité intellectuelle*". According to a recent study (J.L. Aubert, 'Caducité par voie de conséquence dans un ensemble contractuel indivisible', comment to Cass. Civ. 04.04.2006, in *Répertoire du Notariat Defrénois*, 2006, 1194), the former expression « *signifierait que le seul constat du lien de nécessité unissant deux contrats suffirait pour les rendre indivisibles et à en solidariser la destinée, alors même que l'une des parties serait demeurée dans l'ignorance de cette relation nécessaire* ». On the contrary, the '*indivisibilité intellectuelle*' is based on the parties' wills.

<sup>70</sup> See L. Bigliuzzi Geri, 'Risoluzione per inadempimento', in M. Franzoni (ed.), *Commentario Scialoja - Branca*, (Bologna-Roma: Zanichelli, 1988), II, 47. For Italian jurisprudence see Cass. 11 marzo 1981, n. 1389; Cass. 5 giugno 1984, n. 3397.

<sup>71</sup> See in France, Cour de Cassation 13.06.2006, n. 04-15.456.

<sup>72</sup> Examples are financial transactions linked to exchange products or services. Here the link is often instrumental but does not amount to the creation of a network where there is a functional interdependence.

easy distinguishable from a series of independent, yet linked, bilateral contracts<sup>73</sup>. On the other hand, the distinction between linked contracts, characterized as a network, and linked contracts, which parties want to correlate without creating a network, may also be hard to perceive. These are different from two linked contracts for sale where, for example, the seller of house A wants to buy another house, to be paid with the money he gets from buyer B. Certainly, A can only buy the house from C if he sells his own house to B but the two contracts do not constitute a contractual network. The linked contract model differs from that of a contract for the benefit of third party which may permit the creation of a network.

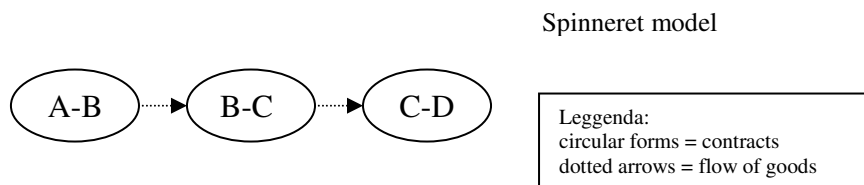
There are two symmetrical dangers that emerge in the current understanding of these phenomena: one is to miss the existence of linked contracts and analyze these contracts as separate, independent and autonomous. The opposite and symmetrical risk is to reach the conclusions that linked contracts should be treated as a single contract. The main aim of this contribution is to show that neither approach is satisfactory and that it is necessary to give legal status to contractual networks as an hybrid form of contractual relationship.

*i. A sketchy taxonomy*

There are at least three different linked models :

Spinneret model

Table 5



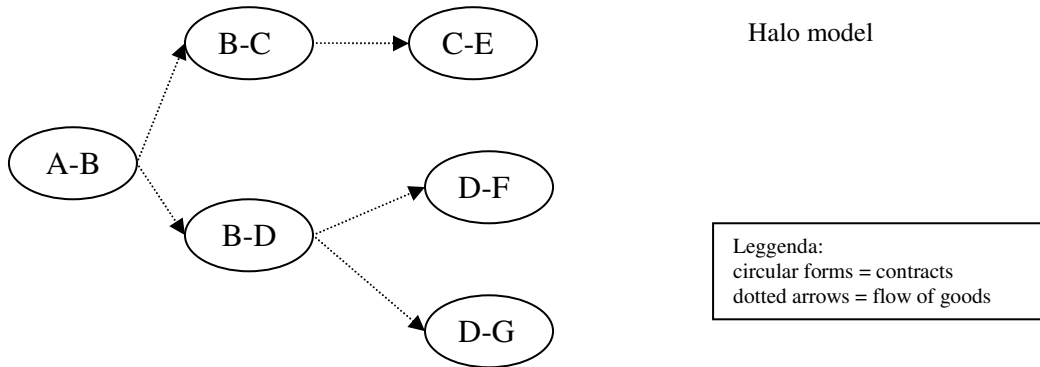
In this model, coordination through voluntary links is easier. If A and B want to achieve a certain result they may agree that B will be bound to insert the clause in the contract with C and impose upon C that he will do the same with D and, in turn, that D will do the same with E.

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<sup>73</sup> The idea of the “contratto complesso”, as a distinct hypothesis from the so called contrats interdépendants (indivisibles), does not apparently play a significant role in the French legal debate. Nor can this idea, as developed by Italian judges (a contract with multiple “cause”), be found in the decisions by the English courts, considering that the category of the “causa” (in Italian), “cause” (in French), on which the concept of the “contratto complesso” is based, is not used in that legal system. See for the Italian case law, Cass. 28.6.2001, n. 8844.

Halo model

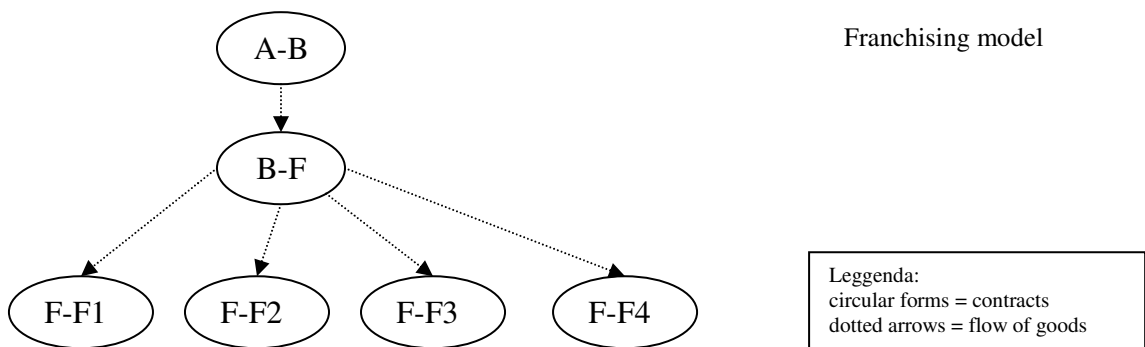
Table 6



In this case, coordination might be more difficult. A can impose upon B the obligation to introduce clauses in its contracts with D and C. However, if C and D want to coordinate with E, F and G, without the mediation of B they might have to resort to an ‘implicit contract’.

Distribution or franchising model

Table 7



Parties’ ability to establish links between different contracts in order to create a network also subtly differ in relation to the structure of the network - whether as a halo or spinneret - and in relation to the time sequence.

ii. A brief comparative overview

Often legal systems associate different consequences with voluntary and necessary contractual links<sup>74</sup>. In particular, the relevance of this distinction concerns interpretation, validity, liability and remedies, and termination among other things. In both cases of voluntary and necessary links, the extent of interdependence among contracts varies quite significantly in national legal systems. These divergences pose serious problems for the legal regimes of trans-European contractual networks and for the application of private international law rules.

In this section, I try to sketch the main differences concerning contractual interdependence in some EU legal systems. The aim is to illustrate the existence of divergences which may hinder transnational cooperation among enterprises if no appropriate legal responses are provided at EU level.

At the outset, it is important to underline the difference between interdependence of performance (*prestations* or *prestazioni*) within one contract and interdependence among contracts or performance within different contracts. For those legal systems that recognise this distinction, the question becomes, whether remedies concerning contractual synallagma can be applied to multiple contracts, thereby defining them as triallagma or multiple synallagma<sup>75</sup>. For example, given two contracts, one between A and B, and the other between B and C, whether the material nature of the breach in the former contract should be evaluated also in the light of the effects produced in the latter; or whether the breach in the former contract could ground the refusal to perform in the latter contract, due to the connection existing between the contracts<sup>76</sup>.

<sup>74</sup> See for the Italian system the distinction between ‘collegamento necessario’ and ‘collegamento volontario’. G. Ferrando, ‘I contratti collegati’, in *Giur. Sist. Dir. Civ. e Comm. diretta da Bigiavi*, (Torino: Utet, 1991); M. Nuzzo, ‘Contratti collegati ed operazioni complesse’, in AA.VV., *Collegamenti negoziali ed operazioni complesse*, (Milano: Giuffrè, 2007), 43 ff. Nuzzo describes the distinction between ‘concorso’ and ‘continuità di contratti’ similar to the French distinction between ‘chaîne’ and ‘groupe de contrats’.

In the Italian legal system, judges distinguish also between *collegamento occasionale* (casual link) and *collegamento funzionale* (conscious link), defining the former as ‘il collegamento deve ritenersi meramente occasionale quando le singole dichiarazioni, strutturalmente e funzionalmente autonome, siano solo casualmente riunite, mantenendo l’individualità propria di ciascun tipo negoziale in cui esse si inquadrano, sicché la loro unione non influenza la disciplina dei singoli negozi in cui si sostanziano”, while the latter appears when “diversi e distinti negozi, cui le parti diano vita nell’esercizio della loro autonomia negoziale, pur conservando l’individualità propria di ciascun tipo, vengono tuttavia concepiti e voluti come avvinti teleologicamente da un nesso di reciproca interdipendenza, per cui le vicende dell’uno debbano ripercuotersi sull’altro, condizionandone la validità e l’efficacia’, (see Cass. sez. II, 27-03-2007, n. 7524).

<sup>75</sup> See in Germany, P. Heermann, *Drittfinanzierte Erwerbsgeschäfte – Entwicklung der Rechtsfigur des trilateralen Synallagmas auf der Grundlage deutscher und US-amerikanischer Rechtsentwicklungen* (Tubingen: Mohr Siebeck, 1998), 163-186 (concerning the ‘do ut des ut det’); Id., ‘Die Stellung des multilateralen Synallagmas im Recht der Vertragsverbindungen’, in *KritV*, 2006, 173.

<sup>76</sup> Some rules stated by French judges seem to confirm that, in the hypothesis of a network of contracts, functionally interrelated, the boundaries of the synallagma correspond to the combination of the obligations resulting from all the contracts of the network. According to many decisions, who is part of the contract functionally linked to a breached contract is admitted to raise the so called *exception d’inexécution*, so as to regain the freedom from a duty of performance which has lost its economic meaning because of the breach of the interconnected contract. See Cour de Cassation, Comm., 15.10.2002, n. 99-21.855; Cour d’Appel, Aix En Provence, 11.10.2005, N. JurisData 2005-291606,

One distinction, more developed in some legal systems than in others, is that between unilateral and mutual dependence. There is unilateral dependence when there is one principal contract, while the others are ancillary, due their function dependence on the principal. On the contrary, there is mutual dependence when each contract cannot achieve its goals without the existence of others<sup>77</sup>.

As already mentioned, the freedom of contract allow the parties to establish contractual links voluntarily, but also that, symmetrically, they may exclude the existence of such links, by fragmenting unitary economic activities. Modifications of contractual links can occur, generating the dissolution of the network, e.g., when parties establish the links and then dissolve them without necessarily terminating their contractual relationships.

What are the rationales for limiting parties' freedom to define contractual interdependencies through links? A relevant issue is represented by the principle of privity or '*relativité des effets*'<sup>78</sup>. Legal systems with stricter notions of privity, limit parties' ability to impose the insertion of clauses in other contracts. However, this limitation refers mainly to those links based on contractual clauses which do not condition the contract where they are included, but are used by parties to regulate and influence another contractual relationship, whose parties differ from those of the first contract.

An important distinction is the one between positive and negative effects on third parties<sup>79</sup>. If the clause inserted in the contract between A and B would produce negative

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whose clear meaning in favour of an *exception d'inexécution* in case of breach of one of the linked contracts can be appreciated through a simple "*a contrario*" reasoning. The adequacy of a concept of multiple synallagma, as an expression suitable to convey the idea of the expanded dimensions of the synallagma in the case of a network of contracts, is confirmed also by a decision taken by the Cour d'Appel di Besançon (14.12.1994, n. JurisData 1994-051501) opting for the remedy of the *résolution* with regard not to the single contract, but to the *ensemble contractuel* as a whole.

See for the Italian legal system, the application of the so called '*exceptio inadempti contractus*', ex art. 1460 c.c., can be used not only in case of a breach in the principal contract, but also the breach occurs in dependent contract. See Cass. 14.01.1998, n. 271; Cass. 19.12.2003, n. 19556; Cass. 28.05.2003, n. 8467; Cass. 11.03.1981, n. 1389; Cass. 16.10.2003, n. 15482.

<sup>77</sup> See that, in Germany, this distinction has only recently been made by the courts. It only plays a role for determining the requirement of contractual form. Otherwise, this distinction is irrelevant. In fact, as opposed to French (Art. 1169-1171 Code Civil) and also Roman law, conditions are permitted to a very large extend. They may even depend on the will of one of the parties, subject to some good faith exceptions. Therefore, it is possible to link contracts either to the will of third parties or to any external event – be it unilaterally or bilaterally. See Bayerisches Oberstes Landesgericht (BayObLG), Judgment of 11 May 1995, *Neue Juristische Wochenschrift – Rechtsprechungsreport (NJW-RR)* 1995, 1167; H.-P. Westermann, in: *Münchener Kommentar zum BGB*, 5<sup>th</sup> ed. (2006), vol. 1/1 "BGB Allgemeiner Teil", § 158, para. 18; Jauernig, in: Jauernig, *Kommentar zum BGB*, 12 ed. (2007), § 158, para. 3.

<sup>78</sup> For a comparative overview see S. Vogenauer, 'Gli effetti dei contratti verso i terzi - L'avant-projet in una prospettiva comparatistica', in M. Andenas, S. Diaz Alabart, Sir B. Markesinis, H. Micklitz, N. Pasquini (eds.), *Liber amicorum Guido Alpa, Private law beyond the national systems*, (London: British Institute of International and comparative law, 2007), 100 ff. Vogenauer examines the analogies but also the differences concerning the principle of *relativité* and privity in western legal systems.

In the French legal system, the principle is stated by art 1165 c.c. As C. Larroumet (*Les obligations. Le contrat in Droit Civil*, (Paris : Economica, 2003), 910) explains, '*le principe de l'effet relative des contrats signifie qu'un contrat ne peut créer de droits et d'obligations qu'au profit et à l'encontre de ceux qui y sont parties pour avoir donné leur consentement*'. In the Italian legal system, see art. 1372 c.c.: '*il contratto non produce effetti rispetto ai terzi*'. See M. Franzoni, 'Degli effetti del contratto', cit.

<sup>79</sup> In English law the terminology is detrimental and beneficial effects for third parties.

effects on the contract between C and D, and also on their contracting powers with other participants to the contractual network, then it is likely to be forbidden (or at least limited). On the contrary, more leeway is given to clauses that would benefit third parties, belonging to the network by conferring rights or limitation of liability.

There are other reasons for constraining parties' ability to separate contracts that might be described as unitary<sup>80</sup>. Often fragmentation occurs to avoid the application of labour law protection or tax law<sup>81</sup>. In this case, contracts are often considered indivisible, despite the presence of explicit contract clauses that point to the opposite direction. The scrutiny would often be made under the public order policy frame.

A few illustrations about national divergences may help identify the main deficiencies and the desirability of a set of European principles concerning the governance of contractual networks of SMEs at European level.

Differences relate, in particular, to the criteria employed to identify the links among contracts, the adoption (plausibility) of "objective" criteria based on the concrete recognition of a complex unitary economic operation, the power of parties to define these links and their ability to apply them to contract with third parties, the consequences in terms of invalidity, termination, rescission, choice of remedies, and, specifically, between damages and specific performance.

The first issue to be analysed is the power to establish and to exclude the existence of contractual links. Interests to recognise or to exclude the existence of contractual interdependence and, thus, of a contractual network may diverge<sup>82</sup>. Often litigation arises to prove the existence of the network, or some particular correlation among contracts. Convergent or divergent interests may also relate to the dissolution of the network, for instance, where a breach or a rescission may make participation in the network detrimental for some parties and beneficial for others<sup>83</sup>.

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<sup>80</sup> In England see *Kilcarne Holdings Ltd. V. Targetfollow (Birmingham) Ltd* [2004] EWHC 2547.

<sup>81</sup> In many cases, English Courts insist on the existence of a single complex economic operation, artificially divided by parties into more contractual acts by parties, in order to elude tax legislation (*Mirant Asia-Pacific Construction Hong Kong Ltd v. Ove Arup & Partners International Ltd*, [2007] EWHC918,TCC; *Philips and another v. Brewin Dolphin Bell Latrie Ltd*, in [2001] 1 W.L.R. 143.

<sup>82</sup> For the German legal system, see, for example, Teubner, "Verbund", "Verband" oder "Verkehr", *Zeitschrift für Handelsrecht (ZHR)* 154 (1990), 295, 300-305; Martinek, *Franchising: Grundlagen der zivil- und wettbewerbsrechtlichen Behandlung der vertikalen Gruppenkooperation beim Absatz von Waren und Dienstleistungen* (1987), p. 123 et seqs. (empirical survey of differing economical interests of franchise partners).

In the Italian legal system, this issue has not been faced in caselaw yet. However, the dominant approach provides that the existence of a contractual link, whether the parties has expressly defined it in a clause or not, has to be evaluated by the judges in order to verify if the situation affecting one contract should impact also on the other linked contracts. When the judges verify the existence of the contractual link, in order to transmit the effects from one contract to the other they should also evaluate the strength of such a link: only in case of a connection between the contracts so strong that linked one cannot resist in the absence of the other, then the effects can be transmissible. See C. Costantini, 'La causa: qualificazione e liceità degli accordi', in P.G. Monasteri, E. Del Prato M.R. Maugeri, et al. (eds), *Il nuovo contratto*, (Bologna Roma: Zanichelli, 2008), 239.

<sup>83</sup> In Germany, the existence of diverging interests have been mainly discussed with reference to contracts on bank transfers, where the question arose whether revocation is allowed vis-à-vis other banks in the chain (i.e. not vis-à-vis the contractual partner), see (in favour of such possibility: Möschel, "Dogmatische Strukturen des bargeldlosen Zahlungsverkehrs", *Archiv für civilistische Praxis (AcP)* 186 (1986), 187 (211 et seqs.); contra: Bundesgerichtshof, Judgment of 25 January 1988, *BGHZ* 103,



Another crucial question concerns hierarchy in contractual networks. Hierarchical contractual networks exist when one party has significant market and contractual power, and there can be cases where this party may abuse that power. If such malfeasance occurs in a network context, its consequences may extend well beyond the domain of the specific relationship. However, it may be that while the asymmetry of power is clear in one relationship, i.e., between contractor and subcontractor, it is less clear in the relationship between the subcontractor and its subcontractor. The 'sub-subcontractor' may not be sufficiently protected if the recognition of the contractual network is missing. Control of power and unfairness should enable the striking out of clauses in linked contracts when they express an abuse of contracting power<sup>84</sup>. As we shall see, often, contractual protection is sufficient and many systems use extra-contractual liability to supplement networks' policing.

The French contract system has recognised the relevance of contractual interdependence and, to a limited extent, even that of *reseau contractuel*<sup>85</sup>. Such recognition has been

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143, 145; Häuser, "Der Widerruf des Überweisungsauftrages im Giroverhältnis", *Neue Juristische Wochenschrift (NJW)* 1994, 3121, 3213-3125; Schröter, "Bankenhaftung im mehrgliedrigen Zahlungsverkehr", *Zeitschrift für das gesamte Handelsrecht (ZHR)* 151 (1987), 181, 141 et seq.

In France, the recognition of a group of contracts, especially of an *ensemble contractuel indivisible* (see *infra*), implies some important consequences, suitable to impact significantly on the business of the parties: firstly, the circumstance that the unenforceability of one contract of the *ensemble* can make unenforceable the other contracts; furthermore, the necessary interpretation of the contracts as a whole, so that each firm of the contractual network has to perform coherently with what stated not only in the contract whose is a formal party, but also with what stated in the other agreements. The fact that the existence of an *ensemble contractuel* is not necessarily beneficial for all the parties is demonstrated by the attention used by judges to evaluate the fairness of the so called *clauses d'indivisibilité*, especially in the employment contracts. Through these clauses, parties expressly define their contracts as an *ensemble indivisible*. But this might be quite "dangerous" for the employee, i.e. the weaker party, seeing that it would certainly increase the instability of the relationship (if not balanced by proper mechanisms). For these reasons, in some cases, the Cour de Cassation has denied effects to *clauses d'indivisibilité*, because they have been judged as abusive. The arrêts mainly regard employment contracts, which are a typology of contracts quite different from the business contracts we are interested in. Nevertheless, they can provide an useful example. See Cour d'Appel Metz (Chambre Sociale), 24.01.2007, n. Juris Data 2007-329442; Cour d'Appel Bordeaux, 3.10.2006, N. JurisData 2006-321494; Cour d'Appel Nancy, 21.06.2006, N. JurisData 2006-313498; Cass., Sociale, 12.07.2005, n. 03-45.394.

See in a case of a withdrawal from a contract linked with others in an unitary economic operation, Cass. 16.10.2003, n. 15482.

<sup>84</sup> See F. Cafaggi, 'Interrogativi deboli sul terzo contratto', in G. Gitti e G. Villa (eds.), *Il terzo contratto*, (Bologna: Il Mulino, 2008), 301. French Courts do not usually apply the consumer protection laws to the contracts B2B. This does not mean that the fairness of the clauses inserted in those contracts is not controlled. Sometimes, judges, called to pronounce on B2B contracts, measure the coherence of the single clause with the so called *économie générale du contrat*, in order to select and eliminate clauses which contradicts this parameter. Some Authors sustain that when the contract B2B is part of a more complex *ensemble contractuel*, the coherence of the single contractual provision will have to be evaluated with regard not only to the "*économie*" of the contract where it is inserted, but to the "*économie*" resulting from all the contracts functionally linked. See A. Constantin, 'Comment to Cass. com., 15 févr. 2000, Sté CMV Financement c/ M. Soulard', in *La Semaine Juridique Ed. Gen.*, 46, 15.10.2000, I, 272.

<sup>85</sup> See S. Pellé, *La notion d'interdépendence contractuelle*, (Paris: Dalloz, 2007); C. Aubert de Vincelles, 'Réflexions sur les ensembles contractuels: un droit en devenir', in *Revue de contrats*, 2007, p. 983, M. Bacache-Gibelli, *La relativité de conventions et les groupes de contrats*, these Paris II (Paris: LGDJ, 1996). The first monograph is Teyssié, *Les groupes de contrats*, Bibl. De droit privé, (Paris: LGDJ, 1975), 139.

framed within the limits of art. 1165 c.c. concerning the so called “*principe de l’effet relatif des contrats*”, according to which “*les conventions n’ont d’effet qu’entre les parties contractantes*”<sup>86</sup>. In particular, the distinction between ‘*chaîne de contrats*’ and ‘*ensemble contractuel*’ distinguishes two different typologies of contractual links<sup>87</sup>. In *chaîne de contrats*, distinguished between homogenes and heterogenes, the content of the contract (*objet*) is the same. In the *ensemble contractuel* the link is established in relation to ‘cause’<sup>88</sup>. The closest notion to the contractual network is that of ‘*ensemble contractuel*’<sup>89</sup>. Within this concept a key distinction is between divisible and indivisible contracts<sup>90</sup>. Indivisible contracts are those where the level of interdependence is higher and, therefore, where events concerning one contract are highly likely to affect the others. The recognition of the ‘complex economic operation’ grounding the *indivisibilité* triggered a deep debate concerning the revision of the concept of ‘*cause du*

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On *reseau contractuel* see D. Ferrier, ‘La consideration juridique du *reseau*’, in *Mélanges Christian Mouly*, (Paris : Litec, 1998), t. II, 95.

<sup>86</sup> See A. Weill, *Le principe de la relativité des conventions en droit français*, th. Strasbourg, (Paris : Dalloz, 1938); J. L. Goutal, *Essai sur le principe de l’effet relatif du contrat*, th. Paris, (Paris : LGDJ, 1981).

<sup>87</sup> See M. Fabre Magnan, *Les obligations*, (Paris : PUF, 2004), 178, on the evolution of *action directe* in *chaîne de contrats*. According to the definition suggested by Teyssie (*Les groupes de contrats*, cit., 39) a ‘*chaîne de contrats*’ occurs ‘*lorsque plusieurs contrats, unis par une identité d’objet, car organisés, a propos d’une même chose, autour d’une même prestation essentielle, sont successivement conclus*’. On the other hand, the expression *ensemble contractuel* refers to a group of contracts which ‘*participent, à titre principal ou accessoire, à la réalisation d’un même objectif*’ (Teyssie, *Les groupes de contrats*, cit., 95). In a few words, the distinguishing element of a *chaîne de contrats* is the fact that contracts, partially or totally, deal with the same goods, or asset or (more generally) property, whereas an *ensemble contractuel* indicates a plurality of contracts sharing a common economic objective (so that a single complex economic operation exists).

<sup>88</sup> Teyssie, *Les groupes de contrats*, Bib. Droit privé, (Paris : LGDJ, 1975).

<sup>89</sup> This concept has been judicially developed unlike that of *group de contrats* which has scholarly foundations. See I. Najjar, ‘La notion d’ensemble contractuel’, in *Mélanges Decocq*, (Paris : Litec, 2004), 509; C. Aubert de Vincelles, ‘Réflexions sur les ensembles contractuels: un droit en devenir’, cit, 987.

<sup>90</sup> J. Moury, ‘De l’indivisibilité entre les obligations et entre les contrats’, in *Revue Trimestrielle de Droit Civil*, 1994, 255. Several years before this study, Teyssie (*Les groupes de contrats*, cit., 107) emphasised the “dichotomy” between *ensemble contractuel indivisible* and *ensemble contractuel divisible*, pointing out that ‘*un ensemble de contrats interdépendants est divisible lorsque l’objectif poursuivi à travers lui est susceptible d’exécution partielle, celle-ci demeurant satisfaisante pour le promoteur du complexe*’. More recently Jean-Luc Aubert (‘Caducité par voie de conséquence dans un ensemble contractuel indivisible’, in *Répertoire du Notariat Deffrénois*, 30.08.2006 n° 15, 1194) has disagreed with this analysis, by arguing that the *indivisibilité* has to be treated as an essential characteristic of the *ensemble de contrats*, in order to associate it with some legal effects. On the basis of an analysis of judge-made law, C. Hannoun (‘Méthodologie d’un droit des montages contractuels’, in *Revue des contrats*, 2007, 3, 1036 et seq.; see, in particular, footnote n. 32), observes a ‘*référence nécessaire en jurisprudence à l’indivisibilité accolée à la notion d’ensemble contractuel qui semble ainsi insuffisante à elle seule à fixer le fondement juridique et les limites de la notion. [...] La référence à l’indivisibilité semble indispensable pour donner un effet normatif tant à l’ensemble contractuel qu’à l’interdépendance*’. Similar conclusions are reached by Aubert de Vincelles, ‘Réflexions sur les ensembles contractuels: un droit en devenir’, cit, 983. It is probably useful to stress that a notion of ensemble contractuel, necessarily related to the concept of *indivisibilité*, can create some problems in terms of stability of the contractual network of cooperating firms, considering that, according to a traditional definition of the *indivisibilité entre les contrats*, whatever affects one contract will make unenforceable the others.

*contrat*<sup>91</sup>, which, according to some, is becoming much more “*pragmatique et économique*”, when compared with the traditional definition. In turn, this change has allowed the *Cour de Cassation* to establish links among contracts and to permit that the invalidity, the rescission or the breach of one contract may affect other contracts belonging to the *ensemble contractuel*<sup>92</sup>. Furthermore, “*la cause*” supplies the theoretical devices to enlarge the concept of synallagma, legitimating, from a systematic point of view, a strong relation between the obligations provided by the different linked contracts. The idea that the boundaries of the synallagma correspond to the combination of the obligations of all the contracts of the network, can be inferred from those decisions, which permit the party of a contract functionally interrelated to a breached contract lawfully to raise the *exception d’inexécution*, so as to be discharged from a duty to perform - the duty having lost its economic meaning because of the breach of the interconnected contract<sup>93</sup>. The role of parties’ intent is relevant both to the inclusion and exclusion of such a link<sup>94</sup>. In order to establish the existence of an *ensemble contractuel*, Courts distinguish between *indivisibilité objective* and *indivisibilité subjective*. Utmost importance is attributed to parties’ will, but, even in the absence of explicit clauses linking different contracts, *indivisibilité objective* can be a sufficient proxy for an *ensemble contractuel*<sup>95</sup>. Indeed, several decisions, especially by the *Chambre*

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<sup>91</sup> See D. Mazeaud, ‘Cause et ensemble contractuel indivisible’, in *Recueil Dalloz*, 2007, 4, 277, commenting on Cour de Cassation Iere, 13.06.2006. But see the critical perspective of J. Ghestin, *Cause de l’engagement et validité du contrat*, (Paris : LGDJ, 2006), and Id., ‘Existence de la cause et perimeter contractuel’, in *Recueil Dalloz*, 25.01.2007, 4, 277.

<sup>92</sup> See M. Fabre Magnan, *Les obligations*, cit. ; J. Flor, J.L. Aubert and E. Savaux, *Droit civil, Les obligations*, vol. 1, *L’acte juridique*, (Paris : Armand Colin, 2006).

<sup>93</sup> See Cour de Cassation, Comm., 15.10.2002, N. 99-21.855 ; Cour d’Appel, Aix En Provence, 11.10.2005, N. JurisData 2005-291606.

<sup>94</sup> Apart from the hypothesis of an express *clause d’indivisibilité*, French Courts tend to convey importance in their reasoning, aimed at affirming the existence of an intention to link, to elements, such as the fact that contracts have been entered contemporaneously or have the same duration, or the fact that the price agreed in a contract becomes reasonable only by considering also the other contracts of the *ensemble indivisible*. See: Cour d’Appel Paris, 27.06.2006, *Sa Axa France Vie c. Corcin*; Cour de Cassation, Comm., 14.01.2003, n. 98.21978, where the Court underlines the elements demonstrating an *indivisibilité conventionnelle de contrats* (and not a merely *indivisibilité objective*); Cour de Cassation, Civ. 3, 20.11.2002, n. 01.10862. An example of the test used by Courts in order to evaluate the existence of an intention to make the contracts indivisible is offered by Cour de Cassation, Comm., 4.04.2006, n. 04-18190.

<sup>95</sup> C. Aubert de Vincelles, ‘Réflexions sur les ensembles contractuels: un droit en devenir’, cit., 983 ff. in relation to Cour de Cassation 15 février 2000. Several decisions, especially by the *Chambre Commerciale de la Cour de Cassation*, seem to develop a more economic-based reasoning, by giving relevance to the objective characteristics of the operation pursued by the contracting parties (i.e. characteristics of the goods, assets, services provided in the contractual agreements). See Cour de Cass., *Chambre commerciale*, 13.02.2007, n. 05-17.407, declaring the existence of an *ensemble contractuel indivisible*, the French High Court emphasises the economic link connecting the contracts: more precisely, the judges observe that one contract would lose its economic meaning (i.e. its economic ratio) if considered independently from the others (i.e. there is not any reference to the different contractual power of the contracting parties). An interesting decision has been adopted by Cour de Cassation, *Chambre Commerciale*, in 1999 (Cass., 15.06.1999, n. 97-12122) where the *indivisibilité* between the *convention de régie* and the *contrat de credit-bail* is affirmed on the basis of the (objective) circumstance that the devices obtained, according to the second contract, could be usefully exploited only in combination with the service provided by the first contract (however, it is true that this is not the only point in the judicial reasoning). In a decision, dated April 4 1995, the Cour de Cassation (Cass. com., 4.04.1995, *Compagnie générale de location c. Kessler*) takes into consideration

*Commerciale de la Cour de Cassation*, have developed economic reasoning, by holding relevant the objective characteristics of the contracts (i.e., characteristics of the goods, assets, and services provided in the single contractual agreements), so as to demonstrate that the performance of one of these contracts, without the performance of the others, will make no sense<sup>96</sup>. In a judgement, the quantity and quality of the investments made by the party of a contract (concluded between A and B), not simply to perform the latter, but also to improve, with the consent of the initial counterparty (B), another contractual relationship (concluded between A and C), suitable for functional combination with the first contract, are considered particularly relevant in order to affirm the existence of a “*lien d’indivisibilité*” between the two contracts<sup>97</sup>.

Can parties intentionally exclude the existence of a single *ensemble contractuel*? Freedom of contract can go both ways: it can establish contractual links or it can separate economically interrelated contracts. Under French law, however, parties have only limited freedom to exclude links. There are hypotheses which consider exclusion of the interdependence ‘abusive’ and, thus, the contracts are held to be interdependent even if parties expressly excluded the link. More precisely, in these cases, judges have stated that the express clause providing that one contract survives the breach (or the invalidity) of the other contracts was contrary to the ‘economic ratio’ of the contract, ‘*en contradiction avec l’économie générale du contrat*’<sup>98</sup>. From this perspective, Courts have been willing to strike down clauses that would uphold debtor’s obligation even if the contract was clearly part of more complex economic activity which was terminated by avoiding or rescinding the other contracts<sup>99</sup>. Obviously, the coherence of the single contractual provision will have to be evaluated with regard not only to the ‘*économie*’ of

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the following situation: a firm, A, after signing an advertising contract with a second firm which controlled a digital resource, reached an agreement with a third operator for the furniture of technological devices, necessary for the digital resource, and a guarantee agreement with a fourth operator according to which the latter would have been a guarantor for A’s liability due to eventual damages provoked to the mentioned technological devices. In this case, *indivisibilité* is justified by judges especially with regard to the functional link between the two contracts (nevertheless, the relevance given to the implicit will, more exactly to the knowledge of the parties about the contractual linkage cannot be denied).

Some French scholars suggest not to overemphasize the dichotomy between *indivisibilité subjective* (or *intellectuelle*) and the *indivisibilité objective*: Aubert (‘Caducité par voie de conséquence dans un ensemble contractuel indivisible’, cit., 1194) notes that: ‘*la chambre commerciale semble adopter une conception de l’indivisibilité plus objective que celle retenue par la première chambre*’. However, ‘*il n’y a pas de véritable opposition dans le concept consacré: les deux formations paraissent bien en adopter une compréhension homogène, notamment en ce qu’elle implique nécessairement la volonté des parties, celle-ci pouvant trouver une confirmation, voire sa révélation, dans des éléments objectifs*’.

<sup>96</sup> See Cour de Cass., Chambre commerciale, 13.02.2007, n. 05-17.407, cit. ; Cour de Cassation, Chambre Commerciale, 15.06.1999, n. 97-12122.

<sup>97</sup> In a less recent decision, by the Chambre Commerciale (Cass. Comm., 11.01.1983, n. 81-14456), the investments made by a firm in order to integrate its business with the activity carried out by other firms, interested to pursue the same economic operation, are taken into the due consideration by judges.

<sup>98</sup> In some cases, the express clause (of severability of contracts) providing that one contract survives the breach (or the invalidity) of the other contracts is held « *en contradiction avec l’économie générale du contrat* ». See Cour de Cassation, 15.02.2000 (N° 97-19.793); Cour de Cassation, Chambre Commerciale, 14.03.2000 (N° 97-11.144). Among the scholars, there is someone who has seen in these arrest one of the first attempts by the French Courts to apply to the contract the powerful devices of the economic analysis of law. The reference is to J.-B. Seube, ‘Opération. Clause d’indivisibilité. Contradiction à l’économie du contrat’, in *La Semaine Juridique Entreprise et Affaires*, 6, 2001, 269.

<sup>99</sup> Cour d’Appel Colmar on 24.05.2007 (SA KBC LEASE France/ LAMBERTS).

the specific contract where it was inserted, but to the ‘*économie*’ resulting from all the functionally linked contracts<sup>100</sup>.

The judicial recognition of *ensemble contractuel* and of the *groupe de contrats* provides a good basis for the recognition of strong interdependence. The consequences of the interdependence may vary in relation to validity and rescission (i.e., withdrawal, termination for non-performance)<sup>101</sup>. A key distinction is the nature of interdependence. In an *ensemble de contrats à dépendance mutuelle*, the invalidity of one contract is ‘transmitted’ to the other linked contracts, thereby giving rise to *anéantissement à cascade*<sup>102</sup>. With regard to the hypothesis of the withdrawal (or termination) of one contract of the *ensemble contractuel à dépendance mutuelle*, the Courts apply the rule according to which “*la résiliation d’un contrat entraîne la résiliation (ou la caducité) du contrat lié*”<sup>103</sup>. In an *ensemble de contrats à dépendance unilatérale*, only the invalidity of the principal contract affects that of the ancillary contracts, but not vice versa<sup>104</sup>. This point ought not to be confused with another aspect which demonstrates the potentiality of the concept of contractual interdependence and which might be expressed through the rule according to which the validity, the conformity of the performance of a contract, i.e., the legal bases of an action claiming the invalidity, or the termination of the contract for material breach, have to be judged by courts not only

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<sup>100</sup>A. Constantin, ‘Comment to Cass. com., 15 févr. 2000 ; Sté CMV Financement c/ M. Soulard’, cit.

<sup>101</sup>Many decisions deal with the question concerning the consequences of the rescission (for breach, frustration, etc) of one contract for the other contracts of the same *ensemble indivisible*. Once the existence of an *ensemble contractuel* is ascertained, the Courts tend to apply the rule according to which “*la résiliation d’un contrat entraîne la résiliation (ou la caducité) du contrat lié*”. Cour de Cass., Chambre Commerciale, 13.02.2007, n. 05-17.407; Cour de Cass., com., 16.10.2007, n. 05-20.395; Cour de Cass., com., 5.06.2007, n° 04-20.380, SA Force micro intégration (FMI) et a. c/ SA Exprim (Juris-Data n° 2007-039235); CA Paris, 28.01.2005, 25e ch. A, SA Grenke location, SA Cybervitrine c/SARL SMC BPC (Juris Data: 2005-266380). Some of the cited arrêts attempt to elect the *caducité*, as the specific remedy which ought to intervene as a consequence of the initial rescission of one contract of the ensemble. J. L. Aubert (‘Caducité par voie de conséquence dans un ensemble contractuel indivisible’, cit.) defines the *caducité* as a ‘*forme d’inefficacité des actes juridiques qui, exclusive de toute idée de sanction, vient prendre en compte un événement postérieur à l’acte valablement conclu et qui prive ce dernier de sa raison d’être*’.

<sup>102</sup>The analysis of the case-law does not reveal many decisions solving the issue of the consequences of the *nullité (absolue or relative)* of a contract on the other *contrats interdépendants*. An example is represented by Cour de Cassation, Chambre Commerciale, 8.07.1970, N° 69-11.545, which solves the legal dispute arising from two contracts, a technology transfer agreement (more specifically a patent licence agreement) and a linked contract for the supply of technical prototypes. The Avant Projet de Reforme, prepared by the Commission directed by Pierre Catala, chooses the *caducité* as the general remedy for the contracts linked to (connected with) the invalid contract (but, apparently, not with the rescinded contract). See *infra*.

<sup>103</sup>See Cour de Cass., Chambre Commerciale, 13.02.2007, n. 05-17.407; Cour de Cass., com., 16.10.2007, n. 05-20.395; Cour de Cass., com., 5.06.2007, n° 04-20.380; CA Paris, 28.01.2005, 25e ch. A, SA Grenke location, SA Cybervitrine c/SARL SMC BPC (Juris Data: 2005-266380).

<sup>104</sup>French scholars speak of unilateral interdependence especially with regard to the link between the *contrat-cadre* and the *contrats d’application*. See Pallaud-Dulian and Ronzano, ‘Le contrat-cadre, par delà les paradoxes’, in *Revue trimestrielle de droit commercial et de droit économique*, 1996, 179. Few decisions regard the consequences of the invalidity of the *contrat-cadre* on the *contrats d’application*. Cour d’Appel, 10.07.1989 (N. JurisData 1989-023627); Cour Cassation, Comm., 3.12.1996, n. 94-10.983. In one decision (Cass. Civ. III, 22.01.1997, n. 94-19.554), we find the expressions *interdépendance unilatérale, lien de dépendance unilatérale* (but see also Cour de Cassation, Chambre Commerciale 8.07.1970, n° 69-11.545).

with reference to the elements of that specific contract, but with reference to the more complex operation. By opting for this logic, the *Cour de Cassation* has overruled a decision taken by a lower Court, since the latter had declared the *nullité* (nullity) of a contract stating the absence of the “*cause*”, without extending its analysis to the whole economic operation of which the contract formed part<sup>105</sup>.

This reasoning has immediate implications for the interpretation of the contracts belonging to the *ensemble*: when interpreting the terms of a contract, the judge ought to consider the ‘economic function’ which this contract is pursuing together with the other *contrats interdépendants*. However, this does not mean that a contract, which is interdependent, must be interpreted by looking to all clauses and terms of the former: otherwise we could risk erring by failing to distinguish the phenomenon of the linked contracts from that of the single complex contract<sup>106</sup>.

When there is an *ensemble contractuel*, remedies that might not been available in the context of bilateral contracts may be employed and, vice versa, remedies available in a purely bilateral context may not be used in a *groupe de contrats*<sup>107</sup>. The presence of an *ensemble contractuel* modifies the applicable law because the interests of parties other than those of that specific contract may be taken into account.

The recent *avant-projet Catala* explicitly recognises contractual interdependence, proposing the introduction of a new article in the Civil Code, to be coordinated with several other provisions that affect rules concerning interpretation, invalidity, liability for breach and other areas<sup>108</sup>. *Contrats interdépendants* are located in Section 7 concerning ‘*les effets des conventions à l’égard de tiers*’. After restating the general principle concerning la ‘*relativité des effets*’ the *avant projet* broadens quite substantially the exceptions<sup>109</sup>. The innovation is strong but somewhat limited by the

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<sup>105</sup>See Cour de Cassation, Chambre Civile 1, 13.06.2006 (N° 04-15.456). For analyses on this decision, see J. Ghestin, ‘Existence de la cause et périmètre contractuel’, in *Recueil Dalloz*, 2007, 4, 277; D. Mazeaud, ‘Cause et ensemble contractuel indivisible’, in *Revue de contrats*, 2007, 2, 256.

<sup>106</sup>Cour de Cassation, Chambre civile 3, 6.11.1996, n. 94-11.808.

Cour de Cassation, Chambre Civile 3, 5.06.1996 (N° 94-16.952, 94-16.971); Cour de Cassation, Chambre sociale, 15.11.2006 (N° 05-42.501); Tribunal com. Paris, 14.10.2003, Mecheri c/ SA Suez (Juris-Data n° 2003-251288) where the liability for *mala gestio*, misleading practices of a corporation with reference to the management of an investment fund has to be appreciated with regard to the fact that the corporation joined a more complex organization, formed by a plurality of parties pursuing the same economic goal, *i.e.* the control of the fund, through the legal infrastructure an *ensemble contractuel*.

<sup>107</sup>See Cour de Cassation Chambre commercial, 5.06.2007.

<sup>108</sup>See *Avant projet de réforme du droit des obligations (art. 1101 à 1386 du Code Civil) et du droit de la prescription* remis au Garde de Sceaux par le professeur Pierre Catala, available at [www.justice.gouv.fr](http://www.justice.gouv.fr). (hereinafter *Avant projet*). Art 1172 of the *avant projet* provides that ‘*les contrats concomitants ou successifs dont l’exécution est nécessaire à la réalisation d’une opération d’ensemble à la quelle ils appartiennent sont regardés comme interdépendants dans la mesure ci après déterminée*’. See the English translation made by J. Cartwright and S. Whittaker.

See J.L. Aubert and P. Leclercq, ‘L’introduction des contrats interdépendants dans le code civil (art. 1172 à 1172-3)’. On these aspects see J.L. Aubert, ‘L’effet des conventions à l’égard des tiers dans l’avant-projet de réforme du droit des obligations’, L. Aynès, ‘Les effets du contrat à l’égard des tiers (art. 1165 à 1172-3 de l’avant projet de réforme)’, both in *Revue de droit de contrat*, 2006, 64; D. Arteil, ‘L’effet des conventions à l’égard des tiers dans l’avant-projet de réforme du droit des obligations’, in *Le Petites Affiches*, 2006, 228, 11.

<sup>109</sup>See art 1165 c.c. of the *Avant projet*.

requirements that interdependence must emerge from clauses inserted in all contracts and be known to the parties<sup>110</sup>. This requirement may for instance prevent a party from using a defence against a third party based on a clause inserted in the contract. For example, a clause limiting liability to the creditor may not be available against the third party if unknown to her, which might usually be the case. This rule would undermine the ability of allocating the risks along the contractual network when there is no knowledge about the contracts. However, if the defendant can show that the third party knew (or could have known) about the limitation, then he can use it as a valid defence.

Interdependence is defined objectively by establishing a necessary link between two or more contracts: there is interdependence when the execution of each contract is necessary to achieve a unitary economic operation. Such interdependence has consequences on the link connecting the validity of one contract to the others belonging to the network. In particular, the judicial notion of *caducité de contrats* (lapse of contracts<sup>111</sup>) would be codified<sup>112</sup>. The codification only refers to *caducité* in relation to *nullité* (nullity), while the judicial use encompasses many other consequences, such as *résiliation* (termination, or withdrawal)<sup>113</sup>.

The *avant Projet* also changes the rule about *cession de contrat* in *groupe de contrats* without the consent of the party whose contract has been transferred. This rule favours ‘internal mobility’ within the *groupe de contrats* and reduces veto power in the interest of the participants.

The German legal system allows a wide range of possibilities for the establishment of contractual links by using parties’ freedom of contract<sup>114</sup>. Parties can link contracts by using conditions, by connecting termination rights, liability exclusions and so on. They can define modes of interdependence both in relation to the creation and the dissolution of the link (*simul stabunt simul cadent, stehen und fallen*)<sup>115</sup>. Limits are in part referred to the principle of ‘*Relativität der Schuldverhältnisse*’<sup>116</sup>.

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<sup>110</sup>See art. 1172.1 and 1172.2 of the *avant projet*.

<sup>111</sup>The expression is used in the English translation of the *Avant-Projet* prepared by S. Whittaker and J. Cartwright.

<sup>112</sup>Cass. Civ. 1 Ch. 4.04.2006, Note Aubert. See art 1131 of the *Avant projet Catala*, see J. L. Aubert, ‘*Caducité par voie de conséquence dans un ensemble contractuel indivisible*’, cit., 1194.

<sup>113</sup>See D. Mazeaud, ‘*Le contrat et les tiers dans l’avant projet*’, cit. p. 683. The most recent decisions which apply the *caducité* to the contracts of the *ensemble* as a consequence of the *résiliation* of one contract of the same network have been already cited in the footnote n. 21: Cour de Cass., com., 16.10.2007, n. 05-20.395; Cour de Cass., com., 5.06.2007, n° 04-20.380, *SA Force micro intégration (FMI) et a. c/ SA Exprim* (Juris-Data n° 2007-039235);

<sup>114</sup>See G. Teubner, *Netzwerk als Vertragsverbund- Virtuelle Unternehmen, Franchising, just in time aus sozialwissenschaftlicher und juristischer Sicht*, cit., and Id., ‘*Coincidentia oppositorum: Hybrid networks beyond contract and organisations*’, cit.; S. Grundmann, ‘*Die Dogmatik der Vertragsnetze*’, *AcP* 207, 2007, 718 and Id. ‘*Vertragsnetz und Wegfall der Geschäftsgrundlage*’, in *Festschrift für Westermann*, forthcoming.

<sup>115</sup>Bundesgerichtshof, Judgment of 8.10.1990, BGHZ 112, 288, 293 (linked franchise contracts); Bundesgerichtshof, Judgment of 24.09.1987, BGHZ 101, 393, 396 (linked construction contract/ deal of real estate); Busche, in: *Münchener Kommentar zum BGB*, 5<sup>th</sup> ed. (2006), vol. 1/1 “*BGB Allgemeiner Teil*”, § 139, para. 18.

<sup>116</sup>For an analysis in comparative perspective of the role of privity see B. Markesinis, H. Unberrath, A. Johnston, *The German law of torts. A Comparative Treatise*, (Oxford: Hart, 2006), 181 ff.

The distinction between unilateral and bilateral interdependence has been used to a limited extent by German Courts<sup>117</sup>.

When parties do not expressly establish the link, German contract law is less keen to identify an indivisible *ensemble contractuel* and apply the principles defined by French Courts within the boundaries of *arrêt Besse*.<sup>118</sup> When a contractual network is established, consequences arise as to information and other obligations grounded on specific contracts, invalidity, termination, and remedies for breach. The requirement of contractual form under § 313 of the BGB has played a major role for the development of contractual links together with the provision on invalidity, § 139 BGB<sup>119</sup>.

Participation in a contractual network may expand the duty to inform beyond the contractual partners. This is an extension of the doctrine of *Vertrag mit Schutzwirkung zugunsten Dritter* (a contract with protective effect advantageous to third parties).

Courts have been holding a party liable on the ground of participation in the network even if the breach had been committed by a different enterprise. In this framework organisational liability has been applied<sup>120</sup>.

In relation to material breach, German Courts have been ready to hold a breach material in the light of the participation of the individual partner in the network. The *Bundesgerichtshof* accepted a relatively minor breach as sufficient justification, given that the quality was regarded as a hallmark of the contractual network.<sup>121</sup> In another

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See that, the principle of the so-called „Relativität der Schuldverhältnisse“ is not expressly laid down in the BGB, but can be derived from various provisions, in particular § 241 para. 1, but also §§ 137, 311 para. 1, 328 and 333. This principle excludes negative effects towards third parties who had not agreed thereupon, whereas positive effects towards third parties are admitted to a large extent (for example: contracts in favours of a third party, § 328 BGB; contracts with protective effect in favor of third parties). See Bundesgerichtshof, Judgment of 23 March 1982, *BGHZ* 83, 257; Kramer, in: *Münchener Kommentar zum BGB*, 4<sup>th</sup> ed. (2003), vol. 2a “Schuldrecht Allgemeiner Teil”, Einl., para. 15; Mansel, in: Jauernig, *Kommentar zum BGB*, 12 ed. (2007), § 241, para. 6; and the monograph by Henke, *Die sog. Relativität des Schuldverhältnisses* (1989).

<sup>117</sup>This distinction has only recently been made by the courts. It only plays a role for determining the requirement of contractual form (for references, see below N. 31). Otherwise, this distinction is irrelevant. In fact, as opposed to French (Art. 1169-1171c.c.) and also Roman law, conditions are permitted to a very large extent. They may even depend on the will of one of the parties, subject to some good faith exceptions. Therefore, it is possible to link contracts either to the will of third parties or to any external event – be it unilaterally or bilaterally.

<sup>118</sup>See for a comprehensive analysis S. Grundmann, ‘Die Dogmatik der Vertragsnetze’, cit., 718 and Id. ‘Vertragsnetz und Wegfall der Geschäftsgrundlage’, cit. See also Section 311, BGB, (obligations created by legal transaction and obligations similar to legal transactions).

<sup>119</sup>See again Bundesgerichtshof, Judgment of 24 September 1987, *BGHZ* 101, 393, 396 (linked construction contract/ deed of real estate). (Only) if the contracts are bilaterally interdependent, the requirement of contractual form will apply to both contracts: Bundesgerichtshof, Judgment of 26 November 1999, *NJW* 2000, 951; in detail: Maier-Reimer, “Die Form verbundener Verträge”, *NJW* 2004, 3741.

<sup>120</sup>See G. Teubner, ‘Coincidentia oppositorum: Hybrid networks beyond contract and organisations’, cit.

<sup>121</sup>BGH, Judgment of 3.10.1984, *Neue Juristische Wochenschrift (NJW)* 1985, 1894; more detail on that decision (rather critical): Böhmer, ‘Recht zur außerordentlichen Kündigung des McDonald’s-Franchisevertrags’, *NJW* 1985, 2811.



case, the termination has been qualified as premature, because of its negative impact not on the specific contractual relationship, but on the whole contractual network.<sup>122</sup>

The recent law reform of the German civil code has introduced the phenomenon of linked contracts (*verbundene Verträgen* or *verbundene Geschäfte*) in § 358 BGB in relation to consumers' rights to withdraw<sup>123</sup>. The reform displays relative continuity with the previous regime, essentially based on previous directives.<sup>124</sup>

In the German courts contractual networks in the form of connected or linked contracts enjoy significant recognition, but limitations when parties have not explicitly expressed their willingness are quite significant.

The Italian model is can be interpreted as stationed between the two previously described and the English model, analysed below. It recognises contractual interdependency but only to a limited extent<sup>125</sup>.

The linked contract model is distinguished from a unitary contract on the basis of substantive rather than formal criteria. The existence of the contractual link is mainly based on three elements: the existence of several contracts (which cannot be unified within a single contract)<sup>126</sup>, the will of the parties to coordinate those contracts towards a common objective (subjective criterion), and the economic and teleological nexus underlying all the contracts (objective criterion). Although in the past the focus was

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<sup>122</sup>BGH, Judgment of 17.12.1998, *NJW* 1999, 1177, where the Court affirmed that termination '*inevitably had a substantial negative impact on the basis of the entire system*'.

<sup>123</sup>G. Teubner has summarised the three conditions necessary to have connected contracts in the following way: "*Together, these three conditions constitute the surplus value of the dual constitution of the connected contracts as against a simple mass of disconnected bilateral contracts within a market*

1. *reciprocal reference of bilateral contracts to one another, either found within the document and/or distilled from contractual practice (multilaterality)*
2. *a contractual reference to the overall project of the connected contracts ( relational purpose)*
3. *a close and significant cooperation relationship between the participants within the multilateral relations*".

See G. Teubner, 'Coincidentia oppositorum', cit.

<sup>124</sup>Clearly, § 358 applies only to consumer contracts. According to this provision, the consumer who is granted a right of withdrawal by other provisions may also withdraw any credit contract which is linked to the contract to be withdrawn. Thus, the rule only concerns withdrawal rights, i.e. the question whether linked credit contracts may be withdrawn if a statutory withdrawal right applies to any single contract. However, para. 3 of the provision has gained some importance for the "general law on contractual networks" insofar as it contains a definition of "linked contracts" (concept of an "economic unit", subject to different requirements where the contracts are concluded with the same or a different partner).

<sup>125</sup>See M. Giorgianni, 'Negozii giuridici collegati', in *Riv. It., Sc. Giur.*, 1937, 334, F. Messineo, 'Contratto collegato', in *Enc. del dir.*, (Milano: Giuffr , 1962), 53. For a complete summary of the case law, see the recent set of contributions published in *I collegamenti negoziali e le forme di tutela*, cit. and before G. Lener, *Profili del collegamento negoziale*, (Milano: Giuffr , 1999).

See Cass. 11.3.1987 n. 2524, and recently Cass. 27.04.2007, n. 7524; Cass. 27.07.2006, n. 17145 (leasing); Cass. 10.10.2005, n. 19678 (agency); Cass. 16.04.2003, n. 7640; Cass. 19.06.2001, n. 8333; Cass. 11.06.2001, n. 7852; Cass. 6.09.1991, n. 9388; Cass. 05.07.1991, n. 7415; Cass. 4.05.1989, n. 2065.

<sup>126</sup>See Cass. 28.06.2001, n. 8844.

mainly on the objective criterion<sup>127</sup>, progressively the concurrence of both the subjective and the objective criteria has been accepted both by scholars<sup>128</sup> and courts<sup>129</sup>. The objective dimension, similarly to the French approach, is associated with the identification of a unitary economic operation based on several linked contracts<sup>130</sup>. Parties have to express, explicitly or implicitly, their willingness and there must be a functional correlation among the contracts so that the linked contract can be described as a unitary economic operation<sup>131</sup>. However, the Italian Supreme Court has recently emphasised that, in case of contracts concluded among different parties (e.g. A with B, and B with C), where the main interest in the existence of the link comes only from one party (in the example B), the parties should either include a clause dealing with such a link within the contract, or, at least, the interested party should make its overall objective known to the others and obtain their acceptance<sup>132</sup>.

A similar distinction to that employed in France between unilateral and mutual interdependence has been developed, in order to isolate the cases in which, for instance, invalidity of one contract can affect also the linked contract<sup>133</sup>.

Once the contractual links have been recognised, then consequences emerge in relation to invalidity, rescission, termination, material nature of the breach, selection of remedies<sup>134</sup>. In case of breach of a linked contract, parties may use the breach as a defence<sup>135</sup>. Materiality of breach can be evaluated in relation to linked contracts<sup>136</sup>, as

<sup>127</sup>P. Senofonte, 'In tema di negozi collegati', in *Dir. giur.*, 1960, 273; E. Zerella, 'Collegamento contrattuale e recesso', in *Rass. dir. civ.*, 1993, 435; G. Ferrando, 'Recenti orientamenti in tema di collegamento negoziale', in *Nuova giur. civ. comm.*, 1997, II, 233; Id., 'Criteri obiettivi (e «mistica della volontà») in tema di collegamento negoziale', in *Foro padano*, 1974, I, 399; Id., 'I contratti collegati', in *Nuova giur. civ. comm.*, 1986, 256.

<sup>128</sup>F. Satta, 'Corrispettività fra prestazioni, collegamento fra negozi, e proroga legale delle locazioni', in *Giur. it.*, 1950, I, 2, 355; ma anche G. Oppo, 'Contratti parasociali', in Id., *Scritti giuridici*, II, Diritto delle società, (Padova: Cedam, 1992), 1; A. Venditti, 'Appunti in tema di negozi giuridici collegati', in *Giust. civ.*, 1954, I, 268; C. Di Nanni, 'I negozi collegati nella recente giurisprudenza (note critiche)', in *Dir. giur.*, 1976, 130; C. Rabitti Bedogni, 'Sul collegamento di atti di società collegate', in *Giur. merito*, 1977, 504.

<sup>129</sup>See Cass. 17.11.1983, n. 6864, and recently Cass. 17.12.2004, n. 23470.

<sup>130</sup>See Cass. 9.4.1983, and also Cass. 17.11.1983, n. 6864, in *Giur. it.*, 1984, I, 1, c. 1460, with a comment of G.P. Cirillo, 'Sul collegamento funzionale di contratti'; Cass. 6 settembre 1991, n. 9388, in *Mass. Gius. civ.*, 1991, p. 1298.

<sup>131</sup>See Cass. 16.02.2007 n. 3645; Cass. 18.07.2003, n. 11240; Cass. 16.10.2003, n. 15482; *Contra* Cass. 25.05.2004, n. 10032.

<sup>132</sup>See Cass. 16.02.2007 n. 3645.

<sup>133</sup>See in general Cass. 28.6.2001, n. 8844; Cass. 27.4.1995, n. 4645; Cass. 4.5.1989, n. 2065. Concerning the extension of invalidity to linked contracts, see Cass. 21.07.2004, n. 13580. On the case of "collegamento funzionale see Cass. 18.01.1988, n. 321; Cass. 30.05.1987, n. 4822; Cass. 17.11.1983, n. 6864; Cass. 5.07.1991, n. 7415.

<sup>134</sup>See Cass. 14.06.2007, n. 13894, where the court denied the transmission of effects concerning jurisdiction between linked contracts, limiting only such transmissibility to invalidity, rescission and termination. See also Cass. 7.2.2006, n. 2598; Cass. 11.4.2001, n. 5371; Cass. S.U. 28.7.1998, n. 7398.

<sup>135</sup>Cass. 14.01.98, n. 271 and Cass. 19.12.2003, n. 19556. The majority of legal doctrine has contended that a party can use breach of a linked contract as a defence. See M. Giorgianni, 'Negozi giuridici collegati', cit., 350; F. Satta, 'Corrispettività tra prestazioni, collegamento fra negozi e proroga legale delle locazioni', cit., 359; A.R. Venditti, 'Appunti in tema di negozi giuridici collegati', in *Giust. Civ.* I, 1954, 271; F. Messineo, 'Contratto collegato', in *Enc. Dir.*, X, 1962, 53; L. Cariota Ferrara, *Il negozio giuridico nel diritto privato italiano*, (Napoli: ESI, 1949), 297.

the courts repeatedly stated that the criteria for evaluating the materiality of the breach include not only the economic value of the performance due, but also the interest of the other party in such performance, and the conduct of both parties within the contract<sup>137</sup>.

The English model is certainly one which has the strongest limitation on acknowledging interdependency. This is partly due to the focus on privity<sup>138</sup>. As we shall see, however, there are different ways of linking contracts: while there are strong limitations concerning the intention of two parties to confer rights or benefits on third parties, there are fewer limitations on the intention of parties to make whole or part of their contract conditional upon other contracts.

The privity requirement is, in principle, still responsible for the narrow recognition of contractual interdependence<sup>139</sup>. To be able to give legal relevance to contractual interdependence different avenues have been used. Parties of the 'principal contracts' have held agents of other contracting parties<sup>140</sup>; a trustee of the third party<sup>141</sup>; a collateral implicit contract has been held between participants to the network which had not signed a specific contract<sup>142</sup>. The Contracts Act of 1999 expands the possibility of a third party beneficiary contract, but does not recognize any form of contractual interdependency similar to '*contrats liés*', '*contratti collegati*' or '*verbundene Verträge*'. The distinction, at the basis of the Act, between beneficial and detrimental effects for a third party clearly defines a framework where the issue is not contractual interdependence, but the effects that one contract can produce over a third party. Certainly one could see the network as the sum of third party beneficiary contracts, but such artificial architecture would contribute little to promoting contractual coordination.

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<sup>136</sup>See G. Lener, *Profili del collegamento negoziale*, cit., 59 and 219. See Cass. 21.02.2006, n. 3742 and Cass. 1 luglio 2005, n. 14034.

<sup>137</sup>See Cass., sez. III, 28-03-2006, n. 7083.

<sup>138</sup>See before the 1999 Act, J.N. Adams and R. Brownsword, 'Privity and the concept of network contract' *Legal studies*, 1990, 12; D. Beylveveld and R. Brownsword, 'Privity, transitivity and rationality', 54 MLR, 1991, 48 and the different view of S. Whittaker, 'Privity of contract and the tort of negligence', in *Oxford Journal of Legal Studies*, 1996, 191 ff.

<sup>139</sup>See Law Commission, 1996. For a short overview see E. McEndrick, *Contract law*, (Basingstoke: Macmillan, 2007), 7<sup>th</sup> ed., 137 ff.; *Chitty on contracts*, Volume I, General Principles, (London: Sweet and Maxwell, 2004), 1073 ff. For a more detailed analysis S. Whittaker, *Privity of contract and the tort of negligence*, cit., 191.

<sup>140</sup>See E. McEndrick, *Contract law*, cit., 162, '*The limitation of the collateral contract device, however is that the court must be able to find evidence upon which to imply such a contract and that consideration must be found to support the collateral contract*'. *Chitty On contracts*, cit., 1076 ff.

<sup>141</sup>See E. McEndrick, *Contract law*, cit., 165 f.

<sup>142</sup>See E. McEndrick, *Contract law*, cit., 163 and *Chitty on contracts*, cit., 709, we read: '*the courts are prepared in some circumstances to treat a statement intended to have contractual effect as a separate contract or warranty, collateral to the main transaction*'. The collateral contract is normally an "implicit contract", strictly linked with another or other "explicit contracts". The collateral contract is economically and legally interrelated with these "explicit contracts". It is between persons, each of one is already bound on the basis of an explicit contract. In other words, there are several contracts which affect the same subject-matter and involve more than two parties (see *Chitty on contracts*, p. 1076). The collateral contract, as an implicit contract, has legal and economic meaning only in connection with the explicit contract. This means that if the latter becomes unenforceable, also the former will lose its effects.

An important case is represented by *Pyrene Co Ltd. v. Scindia Navigation Co. Ltd.*, decided by the Queen Bench in 1954 (see Treitel, *The law of contract*, (London: Sweet & Maxwell, 2007), 678.

The Act recognises the possibility for third parties to enforce a contractual obligation where the contract itself explicitly provides, or when one term of the contract purports to confer a benefit on him<sup>143</sup>. Once the right has been conferred and either assent has been given by the third party or they have relied upon it, then parties cannot modify or extinguish that entitlement. However, this is considered a default rule and parties can modify it by making rescission possible even without the consent of the third party, by introducing a specific clause<sup>144</sup>.

The interpretation so far given by English Courts broadens the range of unexpressed conferral, by creating a rebuttable presumption that parties had introduced terms to confer the benefit on a third party<sup>145</sup>. However, with particular references to contractual chains, courts take a conventional approach and deny the possibility for the land-owner to sue the subcontractor in the construction industry<sup>146</sup>. It is interesting to observe that the Law Commission makes express reference to the practice of the construction industry clearly inclined to reduce sub-contractors liabilities<sup>147</sup>. It is unclear whether in the opposite case, i.e., if the industry practice would so require, the courts would allow liabilities of the contractors against subcontractors located a long way down the chain. Different industries may have different supply chains, design incentives and allocate risks and liability in different ways. A partial answer could be gleaned from a decision, of 2004<sup>148</sup>, rejecting the observation formulated by one party who derived the following principle from the Report prepared by the Law Commission: “*where there is a chain of contracts, a party who is unable to sue on its contract, should not be able to leap up the chain and sue on another contract*”. Cooke J., is explicit on this point:

“The Law Commission report, (...) which in turn refers to the lack of impact of the Act on well-known contractual chains of the kind found in the construction industry with employers, head contractors and subcontractors or in the supply of goods with manufacturers, wholesale suppliers and retail suppliers, does not assist her here any more than in relation to subs. 1(a). Those situations are well-known and provide a commercial background of practice to contracts which are unlikely to cut across the legal framework customarily employed. Here there is no such background. Letters of indemnity take a number of different forms and have given rise to a wealth of arguments between parties on their terms. Each has to be construed according to its own terms”<sup>149</sup>.

The privity doctrine, after the reform, does not provide incentives to creating contractual networks but it certainly does not prevent parties from creating links among different

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<sup>143</sup>See Art 1 Contracts Acts. (Rights of third party to enforce contractual term).

<sup>144</sup>G. Treitel, *An outline of the law of contract*, (Oxford: OUP, 2004), 6<sup>th</sup> ed, 257.

<sup>145</sup>See E. McEndrick, *Contract law*, cit., 146, commenting *Nisshin Shipping Co Ltd. V. Cleaves and Company* [2003] EWHC 2602 Comm.

<sup>146</sup>Law Commission, *Privity of contracts: contracts for the benefits of third parties*, (LC242), 1996, Part VII, (3).1, p. 81.

<sup>147</sup>See in *England Laenthong v. Abdullah Mohammed Fahem &Co.* 2005 WL 986921, [2005] 2 All E.R. (Comm.) 167. What said by the Law Commission with regard to the “construction industry” does not imply that the right of the third to sue will be banned in any chain of contracts: this is the conclusions reached by the Queen’s Bench Division in *Laenthong International Lines Co Ltd v. Artis & Ors*, Nov. 8 2004, [2004] EWHC 2738 (Comm). But see E. McEndrick, *Contract law*, cit., 148 and G. Treitel, *An outline of the law of contract*, cit., p. 256.

<sup>148</sup>*Laenthong International Lines Co Ltd v. Artis & Ors*, Nov. 8 2004, [2004] EWHC 2738 (Comm).

<sup>149</sup>See par. 45.

contracts. Explicit links, where parties may condition the validity, termination or rescission of their contracts upon the validity, termination or rescission of another contract, or even multiple contracts is certainly permissible under English contract law<sup>150</sup>. The major differences with other legal systems relate to the weight attributed to parties' intentions, especially in commercial contracts. Sometimes, however, English Courts, like their German counterparts, infer an intention of parties to link the contracts, using hypothetical reasoning<sup>151</sup>. Contracts are defined as structurally interdependent, because, according to an "ex ante" analysis, it appears that parties would not have entered into one contract without concluding the others. As a result, the termination of one contract brings about the termination of the others<sup>152</sup>. On the other hand, it is undeniable that in these few cases each contract was signed by the same parties: this obviously reduces the interest in these examples, given that the model concerning us is represented by a network of several enterprises (thus, usually more than three), cooperating through bilateral contracts.

A distinct phenomenon is represented by "collateral contracts": here, the judge does not simply infer an implicit will to combine existing contracts; rather, he 'assumes' an implicit contract between parties, of whom at least one is already bound on the basis of an explicit contract with a third party. Therefore, the factual premise is an economic operation involving more than two enterprises. The result is a necessary functional connection between the implicit contract and the express contract(s), in pursuit of the same economic goals. We might speak of unilateral interdependence. The collateral contract is indeed an 'ancillary contract', unilaterally dependent on a 'principal contract', i.e., the express contract. In these cases, English judges tend to allow a transmission of the invalidity (due to illegality) from the principal contract to the collateral contract (not vice versa). Let us imagine the following situation: firm A, interested in developing a product for a new market, enters in a contract with B, who enters in a contract with C for the supply of the raw material. The implicit collateral contract might be established between A and C, as long as C receives specific instructions from A with regard to the kind of material to extract, suitable to optimize A's industrial activity<sup>153</sup>. Nevertheless, it should be noted that, historically, the collateral contracts theory has been essentially used by English Courts as a means of rendering clauses which limit or exclude the liability enforceable by a third party or against a third party. In other words, the collateral contracts device has not been historically exploited to coordinate the performance of a plurality of parties, obliged on the basis of several contracts<sup>154</sup>.

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<sup>150</sup>English contract law distinguishes between contingent and promissory conditions. In this case I am referring to contingent conditions that can be used if parties want to link their contracts to other contracts and make performance conditional upon the performance or validity of other contracts. A case which demonstrates the possibility for parties to explicitly qualify a contract as a *condition sine qua non* for another, distinct contract, is *Gordon Samuel Duff v. Wilfred Egerton*, decided by the High Court of Justice in Northern Ireland, 23.01.2002..

<sup>151</sup>High Court of Justice, Queen Bench Division, Commercial Court, *Maria Elena De Molestina and others Claimant v. Alvaro Noboa Ponton and others* (May 16 2001).

<sup>152</sup>On the contrary, no cases have been detected where the judge, by following the same logical path, extended the invalidity of one contract to the other contracts, linked with the former.

<sup>153</sup>See *Chitty on Contracts*, cit., 1077.

<sup>154</sup>See Law Commission, 19.

*Prima facie*, the English system seems to be less fertile ground for the growth of contractual networks than other legal systems, where contractual coordination is limited but well recognised. Empirical research is needed to verify whether these constraints do really prevent networks from arising or commercial practices have found their ways into innovative forms of contractual coordination even in more ‘conservative’ legal settings.

### 3. *The Disadvantages of Rigid Contract Law for the Creation of Contractual Networks and the Current Institutional Responses at National Level*

Both the multilateral and the linked models face serious limitations under current contract law, more in some legal systems than in others. The costs of rigid contract law, preventing the configuration of interdependent bilateral contracts and limiting the use of multilateral contracts, fosters the use of alternative modes of coordination among enterprises; particularly claims grounded on extra-contractual liability for breaches having consequences on third parties belonging to the network.

A different external solution to a rigid contract law is thus extra-contractual liability<sup>155</sup>. Often legal systems resort to civil liability to extend liability beyond the domain of contractual parties when the effects of the breach by A go beyond its contractual counterpart B and affects C, D, E, all belonging to the contractual network. Given the interdependence among contracts, it is very likely that breaches will often affect other contracts. Extra-contractual liability has been used to grant third parties rights to recover losses based on the contractual breaches of contracts to which they were not privy.

The extra-contractual nature of the claim in subcontracting has been affirmed by the ECJ while interpreting article 5, 1° of the Brussels Convention on contractual obligations<sup>156</sup>. This approach has expanded the role of extra-contractual liability and reduced that of contractual liability, generating some confusion in those countries that admit the *actione directe contractuelle*<sup>157</sup>.

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<sup>155</sup>This issue has been debated in the English context. See in particular B. Markesinis, ‘An expanding tort law -The price for a rigid contract law’, 103 *Law Quarterly Review*, 354; S. Whittaker, ‘Privity of contract and the tort of negligence: future directions’, cit., 191 ff. In France also the limits of *action directe* have contributed to the use of extra-contractual liability. On *action directe* C. Jamin, *La notion d’action directe*, LGDJ, 1991. See also, M. Fabre Magnan, *Les obligations*, cit., 465 ff. ; G. Wicker, ‘La sanction délictuelle du manquement contractuel ou l’intégration de l’ordre contractuel à l’ordre juridique général’, *Revue des contrats*, 2007, 593. For a comparative analysis of the French and the English system see S. Whittaker, ‘Privity of contract and the law of tort: the French experience’, 15 *OJLS*, 1995, 327. In Italy, see. F. Cafaggi, *Interrogativi deboli sul terzo contratto*, cit.

<sup>156</sup>See C-26/91, *Jakob Handte & Co. GmbH v Traitements Mécano-chimiques des Surfaces SA*, [1992] ECR I-03967 ; C-265/02, *Frahuil SA v Assitalia SpA*, [2004] ECR I-01543 ; C-51/97, *Réunion européenne SA and Others v Spliethoff’s Bevrachtungskantoor BV and the Master of the vessel Alblasgracht V002*, [1998] ECR I-06511.

<sup>157</sup>Several decisions, held by French Courts, state that, in the hypothesis of subcontracting chains, the so called “maitre de l’ouvrage” (i.e. the main contractor) can only bring an extra-contractual liability claim (not an *action directe*) against the sous-traitant (the sub-contract). See, for instance, Cass. 3e civ., 11 déc. 1991 : *Juris-Data* n° 1991-003120 ; Cass. 3e civ., 13 mai 1992, n° 90-17.644 ; Cass. 1re civ., 23 juin 1992, n° 91-11.091 : *JCP G* 1992, IV, 2445 ; Cass. 1re civ., 7 juill. 1992 : *Juris-Data* n° 1992-001558 ; Cass. 3e civ., 18 nov. 1992 : *Juris-Data* n° 1992-002519 ; Cass. 3e civ., 22 mai 1996 : *Juris-Data* n° 1996-002150 ; Cass. 3e civ., 5 déc. 2000 : *Gaz Pal.* 2001, 2, p. 1545, comm. V. Roulet ; Cass. 3e civ., 20 déc. 2000, n° 99-11.087 : *RD imm.* 2001, p. 161 ; Cass. 3e civ., 28 nov. 2001 : *Juris-Data* n° 2001-011888 ; Cass. 3e civ., 3 avr. 2002 : *Juris-Data* n° 2002-013887. We could cite, as a paradigm of

In France, the prohibition of ‘*cumul*’ of contractual and extra-contractual liability has necessitated efforts to define the boundaries also in relation to third parties’ claims, stemming from breach of contract<sup>158</sup>. While in France the *ensemble contractuel* has been recognised, narrower limits have been set in relation to contractual claims brought by third parties. After the *arret Besse* the domain of contractual liability has been narrowed and the availability of *action directe* in *ensemble contractuel* reduced<sup>159</sup>. Somewhat paradoxically *action directe* is used more broadly in the context of *chaîne* than in that of *ensemble contractuel*, where the ‘*action delictuelle*’ is preferred.

The *Cour de Cassation* has recently expanded the domain of extra-contractual liability for breach of contract<sup>160</sup>. Third parties, affected by the breach, can bring a claim based on extra-contractual liability<sup>161</sup>. It is clear that this recent evolution will necessitate a rethink of the conclusions reached in 1991 with l’*arret Besse*<sup>162</sup>.

The *avant projet Catala* proposes an important change giving *action directe* broad recognition in article 1168 and, in particular, art. 1342<sup>163</sup>. This proposal would significantly change current French law and will be particularly relevant in *groupe de contrats*<sup>164</sup>. The ability of third parties to bring a contractual claim for breach will ensure consistencies for victims of the same breach, but, even more importantly, will ensure augmented deterrent effects. The contractual claim, unlike damages in civil liability, should – in principle – allow victims of the breach to be placed in the position they would have enjoyed, had the contract been performed. While in many contractual networks specific performance may be preferable, if only damages are available, it is important that they discourage breaches that would have detrimental effects on the network, as well as on individual participants. Better protection of individual parties does not meet these needs, but it is certainly a step in the right direction<sup>165</sup>. The limits to contractual interdependence may affect the applicability of *action directe*<sup>166</sup>.

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this judicial trend, Cass. III, 3 Avril 2002, (N° 00-20.748): « La responsabilité du sous-traitant vis-à-vis du maître de l’ouvrage est de nature nécessairement délictuelle. Viole l’article 1382 du Code civil la cour d’appel qui, pour condamner le sous-traitant à garantir l’assureur du maître de l’ouvrage du paiement d’une somme en indemnisation du préjudice financier subi par le maître de l’ouvrage, retient que les retards de livraison sont de nature à engager la responsabilité des entreprises concernées » ; and more recently, Cass., I, 27 mars 2007, n. 04-20842. On the other hand, the maître de l’ouvrage is usually admitted to promote a contractual liability action against the “fabricant”, supplying the materials (see Cass., I, 9 octobre 1979, n. 78-12502). See also D. Mazeaud, *Les groupes de contrats*, in *LPA*, 05 mai 2000 n° 90, p. 64.

<sup>158</sup>See for example G. Viney, *Introduction à la responsabilité*, (Paris : LGDJ, 1995), 2<sup>nd</sup> ed., 402 ff. ; M. Fabre Magnan, *Les obligations*, cit.

<sup>159</sup>See D. Mazeaud, ‘Les contrat et les tiers dans l’avant projet’, cit., 678.

<sup>160</sup>See D. Mazeaud, ‘Les contrat et les tiers dans l’avant projet’, cit.

<sup>161</sup>See Cassation Ass. Plen. 6 oct. 2006, n°05-13.255, note Viney.

<sup>162</sup>See G. Wicker, ‘La sanction délictuelle du manquement contractuel ou l’intégration de l’ordre contractuel à l’ordre juridique général’, cit., 593, where the Author proposes to broaden contractual liability towards third parties more respectful of the principles of *opposabilité* et *relativité*.

<sup>163</sup>See for the liability regime art. 1342 c.c.

<sup>164</sup>See D. Mazeaud, ‘Les contrat et les tiers dans l’avant projet’, cit., 678, speaks of a *petite révolution* in relation to art. 1342 .

<sup>165</sup>See below the analysis on the specificity of remedies in the context of contractual networks, p...

<sup>166</sup>See D. Mazeaud, ‘Les contrat et les tiers dans l’avant projet’, cit., 681

In the UK, contractual liability to third parties is very limited and generally framed as an exception to the privity principle<sup>167</sup>. Tort law, especially, negligence, can be used to a limited extent by a claimant who has a contract with a party, having a contract with the defendant<sup>168</sup>. The debate has been focussed on the impact of *Junior Books Ltd v. Veitchi & Co* and subsequent case law<sup>169</sup>. The differences with an action in contract law are quite significant: from the liability regime, tort being based on fault, to the necessity that harm has to have occurred, to the recoverable harm<sup>170</sup>. The use of tort law allows claims by third parties even when contractual parties had defined limits to liability. This result, which may be fair, may however also have negative allocative effects, which in turn may force parties when drafting their contracts to discounting *ex ante* the extra-contractual liability caused by the breach<sup>171</sup>.

The use of extra-contractual liability poses more fundamental problems concerning interdependence<sup>172</sup>. To what extent can the use of civil liability internalise contractual interdependence, when the violation occurs? Can the claim for damages pursuant to a breach of contract define the losses associated with contractual interdependence? In terms of deterrence, can the extra-contractual liability be used to stabilise the network and prevent breaches with consequences beyond the immediate contractual partner? How does civil liability protect the collective interest of the network, in particular the reputational concerns? It is reasonable to doubt about the adequacy of civil liability in order to protect interests of individual participants. While the weaknesses of contract law related to protection of collective interest indicate stronger potential for civil liability. Certainly the choice of the network's legal form, whether multilateral or linked, may affect the ability to recover for violation of the collective interest. Similar questions arise in private international law, if *action directe* is not admitted and the only available remedy is extra-contractual liability<sup>173</sup>.

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<sup>167</sup>See S. Whittaker, 'Privity of contract and the tort of negligence: future directions', cit., 212 ff.

<sup>168</sup>On the intersection between privity and tort see S. Whittaker, 'Privity of contract and the tort of negligence: future directions', cit., 191 ff.; McEndrick, *Contract law*, cit., 166 ff.; G. Treitel, *An outline of the law of contract*, cit., 251 ff.

<sup>169</sup>See B. Markesinis, S. Deakin, A. Johnston, Markesinis and Deakin's tort law, (Oxford: OUP, 2007); J. Stapleton, 'Duty of care peripheral parties and alternative opportunities for deterrence', 111 *L.Q.R.*, 301

<sup>170</sup>In English law, for example, but for the doctrine of disappointed beneficiary the injured party cannot claim the losses caused by the breach. In a tort action the party injured by a breach cannot be put in the same position she should have been had the contract been performed. See G. Treitel, *An outline of the law of contract*, cit. p. 252.

<sup>171</sup>The use of extra-contractual liability may be particularly problematic where it re-defines contractual risk allocation that parties have defined. For example, if A and B have limited A's liability to 100 and A's breach affects the costs of B's performance to C's, granting C a claim directly against A may change the balance that parties had defined. In particular, when B and C concluded the contract, they may have defined not only the risks of non-performance by B due to its own 'responsibility', but also those related to external circumstances for which neither party had control, ie A's performance. These arguments should however be compared with those grounded on 'corrective justice'. See S. Whittaker, 'The privity of contract and the tort of negligence', cit., 199. See *Norwich city council v. Harvey* [1989] 1 Wlr 828; *Pacific Associates v. Baxter* [1990] 1 QB 993; *Seeman v. Pilkington* [1988] QB 758.

<sup>172</sup>See F. Cafaggi, *Interrogativi deboli sui fondamenti del terzo contratto*, Il Mulino, Bologna, 2008, p. 00

<sup>173</sup>See C-26/91, *Jakob Handte & Co. GmbH v Traitements Mécano-chimiques des Surfaces SA*, cit.



#### **IV. Contractual Networks and Armonisation of European Contract Law: some Urgent Questions!**

I have addressed the modes of contractual collaboration among enterprises by identifying different models, emerged in some national legal systems. These questions are highly relevant for the growth and competitiveness of European market economy, but have attracted little attention from the authors of the CFR and older proposals such as PECL. They are particularly important for trans-European networks, where enterprises, located in different MSs, wish to engage into a contractual collaboration

I suggest that, especially in globalised and interdependent trading systems, governance of complex contractual networks is an important element which should not be disregarded by European law reforms. It is necessary to point out that in relation to industrial policies, associated with competitiveness, express references to contractual networks have been made<sup>174</sup>. There is a risk that European policies referring to common instruments will be undermined by the use of a concept ( network) which has different width and meanings in national legal systems<sup>175</sup>. Closer coordination between policies and instruments should take place and the debate about the harmonisation of contract law should at least consider two important areas: multilateral and linked contracts, on the one hand, and contracts in regulated markets, on the other hand<sup>176</sup>.

Inclusion of a fully developed regime for multilateral contracts and linked contracts within the wider perspective of contractual coordination in the CFR appears necessary to provide a set of common European principles for the creation of transnational contractual networks. This inclusion will provide a better framework for contractual coordination and a closer link between industrial policies and contractual governance devices.

The recognition of network contracts should take place in the general part of CFR both to develop a specific regime for multilateral contracts, and to ensure that special contract regulations are duly taken into account<sup>177</sup>. While coordination is needed I believe that a separate set of Principles concerning contractual networks should be drafted at EU level<sup>178</sup>.

I would like to provide few examples of a specific set of rules for network contracts, and to draw some general conclusions from the example of franchise regulation as currently proposed in the DCFR.

I) The most significant issue is related to remedies in network contracts. Unlike market contracts, in network contracts, remedies should be devised to protect not only

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<sup>174</sup>See Decision 1639/2006/EC establishing a competitiveness and innovation framework programme (2007-2013), cit.

<sup>175</sup>Differences concern not only legal systems where the concept is underdeveloped, but also economic and social sciences.

<sup>176</sup>See F. Cafaggi, 'Il diritto dei contratti nei mercati regolati: ripensare il rapporto tra parte generale e parte speciale', in *Rivista trimestrale di diritto e procedura civile*, 2008, p. 95 ff.

<sup>177</sup>The issue of linked contract has been addressed by the Acquis principles in relation to consumer contracts, in particular the right to withdraw has been held automatically applicable in linked contracts. In that context an objective definition of linked contract has been adopted with no reference to the intention of the parties.

<sup>178</sup>See below text and footnotes.

individual interests of the participants, but also the stability and effectiveness of the network. These interests, as noted earlier, may not be perfectly aligned. There may be conflicts between an individual participant and the network or there may be conflicts among the participants to the network. In relation to the choice between damages and specific performance, the latter should be preferred over the former when the effects of breach spread onto other network participants. Thus, within the general provisions of DCFR concerning remedies, a new rule should be included granting specific performance when the consequences of the individual breach of contract between two network participants may undermine the stability or the existence of the network itself<sup>179</sup>. In this case, damages to the individual victim may be sub-optimal because they would not capture the ‘collective’ good, i.e., network protection.

The network should be protected, in particular its reputation, independently of that of individual participants. This is certainly true for consortia or joint ventures, where there is a clear distinction between the network and individual participants: Thus in these hypotheses the network as such should be able to file a claim to protect its reputation *vis-à-vis* third parties and members. But the protection of collective interest may be necessary also in contractual networks such as subcontracting or franchising. For example, in franchise even if the trademark is owned by the franchisor, a breach by one franchisee can undermine the reputation of the whole network: the selling of lower quality or defective products not only penalises the franchisor, but also the other franchisees. Currently, many legal systems would not allow the franchisee to sue the other franchisees in contract for breach, but some legal systems allow a tortious claim. The recognition of contractual network in DCFR should enable parties of the network to claim for compensation or for other remedies under contract law – including, in an extreme case, exclusion from the network. Clearly, at the moment, standing varies according to the model: while in the multilateral contract an agent is generally entrusted with a power to bring legal claims on behalf of the network, the same does not happen in the linked model, where, in theory, each participant could act on behalf of the network.

Thus, a general rule should enable the individual victims to claim for remedies that maximize the combined protection of individual and collective network interests, and reflect the ability of the network to protect its own reputation by enabling one party to act on behalf of the network with a collective mandate or an agency contract, either with one member of the network or third parties<sup>180</sup>. Such a rule should enable members of the network to voice their interest in the resolution of the dispute to ensure that potential divergent interests all be represented. A related issue concerns the evaluation of the material nature of the breach. Should materiality of the contractual breach be evaluated in light of its consequences for participants of the network other than the contractual partner? The answer is affirmative, if we consider the necessity to protect with contract

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<sup>179</sup>In relation to the linked contract model, the case law in some member state suggest that there is already some evidence See for Italy Cass. 2 aprile 2001, n. 4812.

<sup>180</sup>In the DCFR the rule should be located in Book III where remedies are defined. One rule should deal with specific performance provision, another rule should be added concerning claims that individual participant or network’s agent can bring on behalf of the network. In France the Avant project Catala specific attention is devoted to remedies in the frame of interdependent contracts.

rules - in addition to those of civil liability, (a) collective and individual interests of the network, and (b) those of the immediately injured party<sup>181</sup>.

II) A second set of issues is related to the definition of unfair terms and practices in contractual networks. Terms or practices which may be considered unfair in bilateral contexts might be thought fair in network contracts, if the participants to the network can benefit from participation in the network. For example, clauses concerning risk allocation may place the burden on some particular knot in the chain but may provide additional benefits to the main risk bearer. A clause to be considered unfair in bilateral contracts may become fair, if the network contracts provide forms of pecuniary or non-pecuniary indemnification or compensation to those who bear higher risks.

III) A third set of issues concerns interpretation of individual contracts in the light of the network contract. Rules of interpretation should change for contractual networks. Both in the case of multilateral contract and that of linked contracts, rules of interpretation should be based on interdependence. They should favour the combination of individual interests with those of the network, conceived as an independent reference point even in the absence of the typical features of limited liability and powers to contract with third parties

IV) A fourth dimension is related to termination, dissolution and post-contractual duties when the contractual network is dissolved. Network contracts, especially those taking the form of a multilateral contract, can be individually terminated or collectively dissolved. In the linked model, theoretically, only individual termination is possible. However, if clauses concerning termination are explicitly or implicitly linked (i.e. *simul stabunt simul cadent* clauses), collective dissolution may also concern that model.

Individual termination is generally regulated in relation to the desire of one party to exit the network be it supply, distribution, or consortium. Termination will have different weight and consequences depending on the identity of the party threatening termination and on the amount of critical resources 'owned' by that party when termination is threatened<sup>182</sup>. Clauses concerning the consequences of individual termination are generally inserted in the contractual network<sup>183</sup>.

It is difficult to design a general provision for termination, given that the level of (specific) investments may vary significantly from contract to contract. Clearly such a rule should balance the legitimate willingness to leave the network, and the interests of the other parties to continue in the cooperative venture. Termination of individual

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<sup>181</sup>See in Italy Cassazione 1 luglio 2005, n. 14034.

<sup>182</sup>For the increasing importance of critical resources in the theory of the firm see L. Zingales, 'In search of new foundations', *Journal of finance*, 2000, 1623. I apply that insight to the issue of contractual network design to suggest that different rules might be needed depending on who possesses critical resources of the network. Notice that this might change over time; thus, especially in supply network where the goal is to produce a new line of products, it might be impossible *ex ante* to define the owner of critical resources and to design a termination rule that would prevent hold-up or opportunistic threat of exit.

<sup>183</sup>In many bilateral contracts clauses concerning repurchase, IPRs are designed to prevent the party from opportunistic behaviour. In network contracts, these provisions assume strategic importance if there is asymmetric allocation of critical resources due to the intentional contractual design or to the way the contractual network has developed over time.

See for example the general provision concerning agency, franchise and distribution proposed in the DCFR book IV-E, I-306 (Stock, spare parts and materials).

participation in the contractual network may trigger negotiations concerning the physical and immaterial asset that the exiting party owns. An important variable is represented by an *ex post* covenant not to compete. Exiting partners are often bound not to engage into a competitive activity. These covenants may affect the ability to use know-how and other material and immaterial assets, and thus are often associated with a clause obliging individuals or the network to repurchase these assets<sup>184</sup>.

A specific question is related to dissolution, i.e., when the participants to the contractual network decide to terminate the network<sup>185</sup>. Here, the regime should be more similar to that of company dissolution, though relevant differences will continue to exist. It is beyond the scope of this essay to deepen the dissolution regime of contractual networks, but the guiding principle should be the influence that such a regime may have on incentives to invest when the network is operating and earlier on when the network is created. This question should not be analyzed only in terms of fairness but also efficiency. Fair distribution of assets in dissolution affects *ex ante* incentives to invest, and thus the efficiency of the network. As economic theory, with some notable exceptions, has clarified, fairness and efficiency are not antagonistic in contract theory.

### 1. *The Specificities of Contractual Networks: the Post Contractual Phase and its Effects on Contract Design*

Contractual networks are certainly long-term and relational contracts in a loose sense. They differ from market relationships because they display a more intense and qualitatively different degree of cooperation associated with the higher level of party interdependency<sup>186</sup>.

Contractual networks are often characterized by a less rigid divide between pre-contractual, contractual and post-contractual stages<sup>187</sup>. Perhaps, the most important difference with long-term contractual relationships is related to the nature of post-contractual duties to cooperate. Contractual networks require parties to cooperate even after individual termination or contract dissolution to protect the common goods and to some extent individual interests.

Individual termination may occur, with different degrees, in long-term relationships. The major differences are associated with the distinction between contracts of definite or indefinite duration<sup>188</sup>. Individual termination can take place in network contracts as well. But in networks, individual termination of contract does not imply the end of the

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<sup>184</sup>See A. Saxenian, *Regional advantages – Culture and competition in Silicon Valley and Route 128*, (Cambridge: Harvard University Press, 1994); R. Gilson, 'Legal infrastructure of high technology industrial districts: Silicon Valley, Route 128, and covenants not to compete', in *New York University review*, 1999, p. 575.

<sup>185</sup>See Cass., sez. III, 28-03-2006, n. 7083.

<sup>186</sup>See O. E. Williamson, 'The Economics of Governance', 2005, cit.; W.W.Powell, 'Neither markets nor hierarchy: network forms of organisation', 1990, p. 300 ff.

<sup>187</sup>For example, in networks parties perceive mutual dependence only *ex post*. See C. Menard, cit., p. 353.

<sup>188</sup>See DCFR, Book III, art 1:109 (Variation or termination by notice).

On unilateral termination M. De Hoon, 'Effective Unilateral ending of complex long-term contracts', ERPL, 2005, 469.

relationship<sup>189</sup>. Post-contractual obligations on individual participants are in place to ensure the stability of the network and to combat opportunistic departures.

To ensure appropriate *ex ante* incentives to cooperate and discourage *ex post* opportunism contractual networks often have post-contractual obligations of confidentiality. Forcing members not to disclose information to third parties, even after termination, allows parties to ensure that cognitive capital, produced inside the network, will not be dissipated even if individual parties decide to quit the networks. Other typical obligations are those related to covenants not to compete or not to use the acquired knowledge in ways that would ‘disrupt’ the cooperative structure of the network. But even positive obligations may be placed on parties after termination in order to preserve the cooperative asset, such as specific clauses or duties to inform.

Even when the overall network is dissolved – thus, when there is not individual but collective termination – parties may be required to cooperate to preserve the competitive advantage generated by the network<sup>190</sup>. Often staging of the contract requires that obligations continue after performance, until the benefits of the cooperative endeavour are captured by the members.

The importance of the post-contractual stage of network contracts can also emerge in the other two models. In the intermediate model, it is often the framework contract that contains post-contractual obligations that bind parties towards members of the network beyond the termination of the bilateral contract. Parties may be bound to cooperate with each other, even after performance is rendered. These obligations can, for example, be associated with the structure of supply chain and require cooperation of the subcontractor when the product reaches further production stages, or even the distribution phase.

Post-contractual obligations owed to parties, other than the contracting partner, can also be found in the linked contract model. For example, in franchising contracts, the franchisee can have obligations towards other franchisees even after the bilateral contract has been terminated. It is clear, in the light of the different models, that the post-contractual stage is much more relevant for the multilateral than for the linked contracts’ model. However, even for the latter it may happen that contractual interdependency not only affects parties during their relationships but after the bilateral contract ends as well. For instance, the obligations of confidentiality that the subcontractor owes to the main contractor may continue even after the contract ends, and within the contractual network may be owed not only to the immediate contracting party but to all or most of the members of the network.

Thus, with different intensity, the three network models examined above display the need for post-contractual obligations to ensure that cognitive and fiduciary capital is preserved and that *ex ante* incentives to cooperate are present.

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<sup>189</sup>About the distinction between network contract and contractual relationship, see, C. Menard, cit., p. 347 ff.

<sup>190</sup>Rules concerning cooperation between the parties in bilateral exchanges are included in the PECL and in the DCFR. In the latter, specific rules concerning cooperation are included within special contracts as those in Book IV-E, art 2:201. No rules concerning cooperation in multilateral contracts are specifically defined. No rules concerning post-contractual cooperation in network contracts are designed.

Therefore, a general rule should be introduced to distinguish between individual termination and contractual dissolution. Of course, a different regime of dissolution should be decided for the multilateral and the linked model. This rule should be complemented with post-contractual obligations that preserve ex ante parties' incentives to invest and ensure sufficiently effective safeguards against opportunistic behaviour.

## V. The Interplay of European Contract Law with Private International Law<sup>191</sup>.

Contractual networks may be formed by enterprises located in different countries and subject to different legal regimes. Transnational European contractual networks have not been specifically regulated by private international law (PIL)<sup>192</sup>. General PIL contract norms do apply<sup>193</sup>. They are based on bilateral exchange contracts which have to be adapted to contractual networks. Here again, the key question is represented by the way PIL regulates contractual interdependence. The obvious distinction is between cases where parties define the applicable law and cases where, in the absence of explicit contractual clauses, the default provisions apply.

It is useful to separate the analysis for the two models considered in this article: the multilateral and linked contracts model.

In the case of multilateral contracts, for example a consortium, a contractual joint venture or an EEIG, several enterprises conclude a contract and define the applicable law according to art. 3 of the Rome Convention or, when it enters into force, Regulation Rome I<sup>194</sup>. According to that provision, parties can choose the law governing the contract<sup>195</sup>. If no specific provisions are inserted, then art. 4 of the Rome Convention, and, when it enters into force, Regulation Rome I, would apply. The default provisions of art. 4 have been transformed from mere presumption into fixed rules. The criteria set out in art. 4 define rules for specific contracts and then general principles for all the other contracts based on the characteristic performance or the closely connected law<sup>196</sup>. Some difficulties might arise in relation to multilateral contracts aimed at coordinating activities of enterprises along the supply chain, as it is the case for consortia or EEIG, for example, the identification of the debtor of the characteristic performance.

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<sup>191</sup>This section draws on a joint paper with S. Clavel, 'Which legal PIL regime for trans-national European networks?', forthcoming, on file with the author.

<sup>192</sup>The matter is currently regulated by the Convention on the law applicable to contractual obligations, Rome 19 June 1980 [OJ 09/10/1980, L 266], and will be regulated by Regulation on the applicable to contractual obligations (Rome I) , 31 March 2008, PE-CONS 3691/07, hereinafter Regulation Rome I.

<sup>193</sup>For a first comment concerning the relationship between DCFR and private international law, see P. Lagarde, 'Cadre Commun de reference et droit international privé', in R. Schulze (ed.), *Common frame of reference and Existing EC contract law*, (Munich: Sellier - European Law publishers, 2008), 263. For a general introduction see O. Lando, 'Contracts', in *International Encyclopedia of comparative law*, vol. III, 19.

<sup>194</sup>From now on, I shall refer only to Regulation Rome I.

<sup>195</sup>See Art 3 (Freedom of choice).

<sup>196</sup>See Art 4.2 and Art 4.4.

In the linked contract model, there are more difficulties. Again we should consider the choice of linking ‘independent and autonomous’ contracts and that of separating contracts, structurally and functionally linked. The focus of this section is on the former, but PIL rules apply also to cases where parties explicitly exclude the existence of links and these clauses may be subject to the scrutiny of *lois de police* if one party has abused of its contractual power<sup>197</sup>. The distinction between links explicitly made by parties and links that may be inferred, despite the absence of explicit clauses, operate also in private international law. Freedom of contract under art. 3 of the Rome Convention and Regulation Rome I gives parties a broad power to choose the applicable law. The main open question is related to the possibility of considering a ‘unitary economic operation’ of linked contracts among enterprises located in different MSs.

Let us assume that there are three contracts between A and B, B and C, C and D. These are all interdependent, but each contract may refer to a different law applying to interdependence, i.e., how each contract will affect and is affected by the other two.

If parties define the applicable law they can coordinate in different ways:

- a) decide to apply the same law to all the linked contracts;
- b) decide to apply different laws, but coordinate them so that interdependency will not be undermined;
- c) decide not to define the applicable law, thus implicitly accepting the default provisions of art. 4.

If parties decide to apply different laws, conflicting criteria may emerge.

For example: A-B is governed by French law; B-C is governed by English law; C-D is governed by Italian law. How does private international law solve the conflict between three conflicting choices concerning interdependence among the contracts?

Suppose that there are three different laws of interdependence concerning invalidity. Just to provide an illustration:

- a) the French law would allow full effects of nullité of contract 1 on contract 2
- b) the Italian law would allow only limited effects of nullité of contract 1 on contract 2;
- c) the English law does not allow any effect, i.e., the invalidation of contract 1 does not affect the validity of contract 2.

Let us imagine that A-B is void. If we apply the French law of interdependence chosen by the parties, the contracts B-C and C-D should be void. If we apply English law to B-

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<sup>197</sup>National legal systems diverge on the applicability to public order and public policy to contracts. On the impact of *lois de police* on linked contracts, there is interesting recent French Case Law on *sous-traitance*. While the Cour de cassation had first decided that the French law of 1975 on sub-contracting (which, among many protecting devices gives the sub-contractor an *action directe* against the *maître de l'ouvrage*) was not a *loi de police* (Civ. 1, 23.01.2007, Bull. I, n°33, obs. I. Gallmeister, *Dalloz*, 2007, 503; note E. Borysewicz et J-M. Loncle, *Dalloz*, 2007, 2008; RDC, 2007, note P. Deumier, 879), it changes its mind at the end of the year 2007 (Ch. Mixte, 30.11.2007, 2007, pourvoi n° 06-14006, note W. Boyault, S. Lemaire, *Dalloz*, 2008, 753; Civ. 3, 30.01.2008, pourvoi n° 06-14641; Civ. 3, 8.04.2008, pourvoi n° 07-10763) where the result is that even if parties decide to explicitly exclude linked contracts, the sub-contractor will be entitled to use *action directe* according to French law acting as *loi de police*, whenever the contract is for the construction of an immovable in France (which by the way is a surprising criterion).

C, that contract should not be void because of invalidity of A-B contract<sup>198</sup>. Different laws of interdependence may bring about different consequences concerning the stability of the network.

Another example concerns the effects of breach on third parties and their ability to bring a claim in contract or civil liability. The same breach by B in the first contract may give rise to a contractual claim by C, if French law is applied where *action directe* is admitted, and to an extra-contractual claim, where *action directe* is not admitted as in England or Italy<sup>199</sup>.

How can we solve the conflict between two different choices of applicable law concerning interdependence (i.e., the law applicable to interplay among two or more contracts when one is invalid, terminated, or breached and these legal events affect the other contracts)?

Art. 3 defines freedom of contract as the main criterion, and then identifies some limitations. Accordingly, parties are able to define the law of interdependence that best suits them. The law determining interdependence might be different from that governing the contract 'in general'. Parties can only do that to a limited extent under the current interpretations of art 3. of the Rome Convention. Given the debate on the limits of *depeçage*, it is questionable whether parties would be able to submit interdependence to a given law, if other questions, like the remedies, were be ruled by a different law. If the 'law best suited to interdependence' is French law, but the best for remedies in that specific case is German law, parties are often asked to select either one<sup>200</sup>. If no specific clause determines the law applicable to the question of interdependence, then the substantive law will depend on the law applicable to each contract, following the criteria set out in art. 4 of Rome Regulation I<sup>201</sup>. If the criteria set out in arts 4.1 and 4.2 are not applicable, the close connection criterion should be applied<sup>202</sup>. References to an escape clause if there is a strong relationship among contracts is made in art. 4.3 and in the Recital of Regulation Rome I<sup>203</sup>.

If the rule, once in place, will be uniform across MSs, its application will probably not be homogeneous as its predecessor. This, in part depends on different substantive laws applicable to linked contracts. There are different concepts of contractual interdependence in national legal systems and thus they may not be consistent one with

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<sup>198</sup>These statements are gross generalisations meant only to illustrate the point.

<sup>199</sup>See V. Heuzé, 'La loi applicable aux actions directes dans les groupes de contrats: l'exemple de la soustraction internationale', *Revue critique de droit international privé*, 1996, 243 ff. For a comparative account, S. Vogenauer, 'Gli effetti dei contratti verso i terzi - L'avant-projet in una prospettiva comparatistica', cit.

<sup>200</sup>On the limits to *depeçage* and the differences with incorporation by reference, see P. Nygh, Party Autonomy in International Contracts (1999), 122; J. Kropholler, Internationales Privatrecht (2006), 462; M. Windmüller, Vertragsspaltung im IPR des EGBGB und EGVVG (2000), 70 ; P. Stone, European Private International Law (2006), 54, 87-88, 135, 137, 179, 189-190.

<sup>201</sup>Art 4 defines rules for specific contracts and then a default rules for contracts not listed or when the criteria set out would be conflicting. The default rule is that of characteristic performance. See art. 4.2.

<sup>202</sup>In relation to Rome Convention the case law in different MS suggests different interpretations concerning linked contracts. See Cour d'appel Versailles, 6.2.1991, in *Revue critique de droit international privé*, note P. Lagarde, 1991, 745 ; Cour de Cassation, 22.05.2007, note P. Lagarde, 592 ff.

<sup>203</sup>See Recital 20 Rome I Regulation.



the other, if different applicable laws are necessary. Coordination of applicable laws, so as to ensure that interdependence is guaranteed, should be pursued.

Suppose we have three contracts A, a German seller, sells to B, a French buyer, raw material to be transformed and sold to C, an Italian manufacturer, who has concluded a distribution agreement with D, an English distributor. In this case, unlike the foregoing, parties do not indicate applicable laws in their contracts. If no specific provisions are designed, each contract will have an applicable law defined according to the general criteria set out in art. 4 of the Rome I Regulation. These criteria are often based on territoriality and define the applicable law according to the place where one contractor has its habitual residence or that where the performance takes place<sup>204</sup>. Those criteria will lead to the application of three different laws: the German in the first contract, the French in the second, and the English in the third. They are based on territoriality, either correlated to the residence of the parties or the place of performance, or close connection to the contract. These criteria do not seem to promote functional interdependence which implies a different analysis. If the contracts are regulated by three different legal systems, contractual interdependence will be regulated in three different ways. It will be very difficult if the first contract is invalid to consider the other two invalid on the basis of the French approach to *group de contrats* and *indivisibilité*, as if the three contracts were all regulated by French law. The distribution contract regulated by English law may not be influenced as much as interdependence would require by the previous two contracts and thus interdependence may be weakened<sup>205</sup>.

In relation to linked contracts some legal systems of European MSs use a hierarchical functional criterion. They identify the principal contract and ancillary contracts and apply to the latter the applicable law of the former<sup>206</sup>. Since no specific references in the Regulation Rome I is made, it is unclear whether national judges will be allowed to use it. The relationship between characteristic performance and closely connected country is highly controversial under Rome Convention and national courts have not interpreted it identically<sup>207</sup>. Moreover, this criterion can perhaps fit contractual networks where there is unilateral dependence; that is, hierarchical networks, but it would not suit those where there is mutual interdependence among contracts which makes it impossible or at least inappropriate, to define the principal and the ancillary.

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<sup>204</sup>See in relation to a distribution contract where the Italian Court has given a relatively peculiar interpretation of art 4 in relation to distribution contract, Cass. Civ. 11.06.2001, n. 7860.

<sup>205</sup>In distribution contract parties are free to choose the applicable law, but if they do not, the applicable law will be that of habitual residence of the distributor, which might not be always the best law to promote the stability of the contractual network. Clearly a functional approach that indicates the applicable law that which best promotes contractual coordination may not be easy to identify.

<sup>206</sup>See for France, Vander Elst, 'Le rattachement accessoire en droit international privé', *Studi in memoria di Giuliano*, for Germany, von der Seipen, *Akzessorische Anknüpfung and engste Verbindung im Kollisionsrecht der komplexen Vertragverhältnisse*, (Heidelberg, 1989). On French Case Law prior to the Rome Convention system: applying the law of the principal contract to the contract for guarantee: CA Paris, 21.05.1957, *Rev. Crit. DIP*, 1958, 128; Civ. 1, 1.07.1981, *JDI* 1982, 148; applying the law of the principal contract to the preparatory contract: see for an architect contract accessory to a construction contract, Civ. 10.07.1990, *Rev. Arb.*, 1990, 854, note Moitry; applying the law of the principal contract to the modifying contract: Civ.1, 25.05.1992, *Rev. Crit. DIP*, 1992, p. 689, note Jarrosson.

<sup>207</sup>For a short comparative analysis see P. Lagarde, note à Cour de Cassation (Ch. Comm.) 19.12.2006, Cour de Cassation 22.05.2007, *Revue critique de droit privé*, 2007, 592.

In trans-European contractual networks similar problems to those envisaged for domestic networks arise. Often, interests within the network are not homogeneous, there is a combination of conflict and cooperation, there must be room for some degree of competition. In the framework of the rules of PIL, it is necessary to distinguish between hierarchical and non-hierarchical networks, to devise rules that, while fostering cooperation among different participants, would ensure sufficient protection to the party with lesser contract and market power.

The logic behind current PIL contractual provisions seems to be partitioning not linking. Even if contracts are interdependent they are broken down into bilateral relationships and the applicable law is defined accordingly<sup>208</sup>. When there are contractual networks, the scope of the decision concerning applicable law should be that of strengthening contractual interdependence; promoting the network stability, or transnational cooperation. Cross-boundary cooperation at EU level should be considered a priority of the new regulatory framework's contribution to the formation of a single European market. This functional approach requires, at least for contractual networks, a specific rule to be added to art. 4, Regulation Rome I and for it to be devoted to European contractual networks. The Small Business Act might be a good opportunity to signal this necessity.

## VI. Preliminary Conclusions and Future Policy Directions

Contractual networks represent an important form of inter-firm cooperation in Europe. They exist in BtoB and BtoC relationships. In this essay, I focused on BtoB and underlined the limited attention that has been paid by recent and more consolidated proposals of law reform of European contract law. While EU industrial policies promote the creation of European networks of SMEs, and these networks are present in many regulated markets from energy to telecom, from banking to transport and aviation, the legal framework is still organised around the bilateral exchange contract, according to the conventional national legal systems. To make things worse, the proposed draft of Regulation Rome I, which should play a significant role in trans-border BtoB transactions, neglects to regulate multilateral contracts and contractual networks. The lack of legal framework might not only be hindering the development of European trans-border inter-firm collaboration, but it also weakens Europe as a potential supplier of legal models in the worldwide market for efficient contract rules.

The proposed European Small business Act should complement a company law statute for SMEs with Principles of European contractual networks (PECON). Empirical evidence shows that often collaboration takes first the contractual dimension. Only later, when sufficient reciprocal trust has been generated, parties complement the contractual dimension with (partial) ownership integration<sup>209</sup>. In addition rules concerning corporate restructuring and the bankruptcy of enterprises which belong to a contractual network should be devised.

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<sup>208</sup>There is awareness of these limits. See for example Recital 19 of the Regulation Rome I.

<sup>209</sup>See F. Cafaggi and P. Iamiceli, *Reti di imprese tra crescita ed innovazione organizzativa*, cit.

I suggest that it is time to draft European General Principles on contractual networks, fusing the European private law and private international law dimensions. These principles should have soft law form, and be drafted having in mind a multilevel system: i.e., whatever is not explicitly regulated shall be supplemented by national legislation, leaving space for a certain level of differentiation.

These Principles should concentrate on contractual networks and be coordinated with principles of competition law, concerning both horizontal and vertical cooperation<sup>210</sup>.

The structure of such Principles should identify the new roles of contract beyond pure exchange, focusing on organisational and regulatory functions.

The rules should be sufficiently open so as to leave space for judicial interpretation and bottom-up innovation. Parties can refer to these rules and adapt them to their specific needs. An improvement in the efficiency of BtoB cooperation at transnational level would be of service to the public. Though the main aim should be trans-European cooperation the rules should be applicable to domestic networks as well if parties so wish.

In terms of content, they should provide a definition of contractual networks; a specification of a contract for networks, furnishing a general framework to be applied to different forms of collaboration within production and distribution or by linking producers and distributors. The principles should certainly deal with the two models of multilateral and linked contracts, but also go beyond them. In particular, more weight should be given to the principle of reliance in contractual networks. Reasonable reliance can contribute to delineating the boundaries of the network and the often troublesome consequences that each participant can precipitate while acting in the bilateral context. It can also provide incentives for parties to evaluate, *ex ante*, the impact on third parties.

These rules should ensure both the stability and the flexibility of the contractual network. They should prescribe different entry and exit systems accordingly. They should distinguish between internal relationships among members and relationships between the network and third parties, in particular, creditors. They should design different degrees of complexity with increasingly structured forms of governance which may take place inside the network or use companies to perform specific activities requiring limited liability and asset partitioning.

Strategic importance should be devoted to knowledge transfers and innovation. Specific rules should be devised so as to maximise knowledge transfers within the network. Contract rules become extremely important when knowledge cannot be propertized either because no legal devices are available, or because the benefits of sharing are such that a property regime would be inappropriate. Two problems should be addressed in the Principles on European contractual networks:

- 1) Disproportionality between individual investments and profits, granting special protection to those who must make specific investments;
- 2) Unauthorised transfers to third parties, external to the network. Covenants that can ensure strong safeguards against opportunism should be adopted, but often it is within the monitoring system that control over knowledge transfers can occur. Again it is

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<sup>210</sup>Eg: Guidelines on horizontal cooperation address contractual networks, Guidelines on vertical cooperation address contractual networks, etc.

important that protection systems do not ossify the network, reducing flexibility and incentives.

Finally, a special regime concerning trade secrets and IPR should be designed so as to maximize incentives to produce innovation inside the network, but, at the same time, to generate strong safeguards against opportunism and knowledge leakages.

The chance to define these rules at European level and coordinate them with the private international law regime can provide new and stronger competitive tools in the international marketplace. The new European Small Business Act should not miss this opportunity.