Chapter

# France


Rod Cork

Marc Santoni

Allen & Overy LLP / SCP Santoni & Associés


## 1 Issues Arising When a Company is in Financial Difficulties

### 1.1 How does a creditor take security over assets in France?

Security over assets is taken by the entering into of a security agreement between the grantor of the security and the creditor or class of creditors benefiting from the security.

Separate security agreements will generally be required for each class of asset to be secured. The general business charge (*nantissement de fonds de commerce*) in France is much more limited in scope and effect than the common law floating charge.

Perfection of security against third parties will depend on the type of asset secured and may include actual or deemed de-possession of the assets by the grantor, written notice, registration with the commercial court of the grantor, and/or with the intellectual property or real estate registry. Some security documents may need to be executed before a notary by way of notarial deed.

The secured debt will need to be determined or determinable in amount at the time the security is taken and, for certain types of security, there are statutory limitations on the amount of debt which can be secured and on which creditors can be the beneficiaries of the security. Where security is registered, this may be required to be renewed periodically to maintain the security interest in force.

It is generally possible for different classes of creditors to be secured in different orders of priority on the same assets in France. It is customary in France for such secured creditors to enter into a priority agreement organising their inter-creditor relationship with respect to any such security and the ranking of enforcement recoveries.

In order to enforce security in France, it will be necessary to demonstrate that there has been a payment default. Enforcement will usually be made by way of public auction or sale of the secured assets. For certain types of secured assets, French legislation now provides that parties may agree to include in the security agreement an expedited form of private sale (*pacte commissoire*).

The opening of Safeguard (*procédure de sauvegarde*) or Reorganisation (*redressement judiciaire*) by a company which has granted security will generally prevent enforcement of that security during the observation period following the opening of such proceedings. Security which has been granted in the insolvency "suspect period" (see question 1.2 below) may be declared null and void.

### 1.2 In what circumstances might transactions entered into whilst the company is in financial difficulties be vulnerable to attack?

Transactions entered into by the debtor during the "suspect period" may be void or voidable in certain circumstances. The suspect period starts at the date of cessation of payments and ends on the date on which the court orders the opening of the insolvency proceedings. The suspect period cannot exceed 18 months except for certain gratuitous acts when it may be extended by the court for an additional period of up to six months. There is an unlimited suspect period for certain intentionally fraudulent or collusive transfers.

When declaring a company insolvent, the court determines the length of the suspect period. The court can, on its own motion or at the request of the administrator, the creditors' representative, the liquidator or the public prosecutor, revisit and set a new date of cessation of payments. In Safeguard, there is no hardening period and transactions cannot be set aside during these proceedings.

The types of transactions mentioned below apply if a company goes into Reorganisation or Liquidation. French law distinguishes between two categories of vulnerable transactions: transactions which must be avoided by the court if certain legal requirements are met; and those which may be avoided depending on the knowledge of the person dealing with the debtor. In both cases, the claimant does not need to demonstrate that the act prejudices the insolvent company.

Transactions which are null and void include, for example, all gratuitous acts which result in a transfer of real or personal property (this includes all forms of gifts or transactions for no consideration), any bilateral contract under which the obligations of the debtor significantly exceed those of the other party, any payment made (in whatever way) in respect of a debt which has not yet fallen due for payment, and any mortgage or pledge over the assets of the debtor granted for existing indebtedness.

Transactions which are voidable include, for example, payments in respect of due debts made from the date of insolvency, and onerous acts performed after that date, if the persons dealing with the debtor company were aware of its insolvency at the time.

The Financial Collateral Directive, as implemented in France, could have an impact on any avoidance provisions involving financial collateral.

### 1.3 What are the liabilities of directors (in particular civil, criminal or disqualification) for continuing to trade whilst a company is in financial difficulties in France?

The term "directors" includes not just directors given the title of director, but also shadow or de facto directors (*dirigeants de fait*). In accordance with case law and French commentators, de facto directors are "persons who, without having the quality of being legal directors, have positively intervened in the direction and management of the legal entity, with all sovereignty and independence, in order to directly influence the same in a determined manner".

Directors of an insolvent company can face various charges of civil and/or criminal liability in France including the following:

- Deficiency of assets (*responsabilité pour insuffisance d'actifs*)

When the resolution of a Safeguard scheme, the resolution of a Reorganisation scheme, or compulsory Liquidation results in a deficiency of assets if there is proof of a management error having contributed to the deficiency of the assets, for example the perseverance in the continuation of a loss-making where there is no possibility of restructuring.

- Personal bankruptcy (*faillite personnelle*)

At any stage in Reorganisation or Liquidation, for example where the director has made purchases in order to resell below market price, or has used inappropriate methods of raising funds, with the intention of avoiding or delaying the opening of formal insolvency proceedings or he has paid, or caused to be paid, one creditor in preference to others after the cessation of payments and with knowledge of the cessation of payments. Personal bankruptcy prevents the director from being involved in the management, administration or control (*directly or indirectly*) of any commercial or business entity or any company engaged in economic activity.

- Criminal bankruptcy (*banqueroute*)

In the event of the opening of Reorganisation or Liquidation, the debtor or its director (if it is a legal entity) may be guilty of criminal bankruptcy if, for example, he has bought goods in order to resell below market price, or has used inappropriate methods to obtain funds, in each case with the intention of avoiding or delaying the commencement of proceedings for judicial reconstruction.

Possible sanctions include a fine, imprisonment, prohibition from managing a company and an order to contribute to the insolvency deficiency.

## 2 Formal Procedures

### 2.1 What are the main types of formal procedures available for companies in financial difficulties in France?

When a corporate borrower faces financial difficulties the following restructuring and insolvency regimes may be applicable under French Law, as follows:

(a) Special Mediation (*mandat ad hoc*).

(b) Conciliation (*conciliation*).

(c) Safeguard (*procédure de sauvegarde*).

(d) Accelerated Safeguard (*sauvegarde accélérée*, the **AS**) from 1 July 2014 and Accelerated Financial Safeguard (*sauvegarde financière accélérée*, the **AFS**).

(e) Reorganisation (*redressement judiciaire*).

(f) Liquidation (*liquidation judiciaire*).

The first two of these proceedings are essentially pre-insolvency proceedings whereas the other proceedings are court-based collective insolvency proceedings.

Special Mediation and Conciliation are not coercive proceedings. Whether a particular regime mentioned above is available will largely depend on whether or not the company is solvent or insolvent (see question 2.2 below). The opening of Safeguard and Reorganisation have important consequences on creditors' rights and remedies.

The AS was introduced by a new reform of French insolvency law that comes from Ordinance n°2014-326 of 12 March 2014 and will came into force on 1 July 2014. The AFS existing prior to this Ordinance will continue to be available until 1 July 2014 but, as from that date, the regime of the AFS will be the one resulting from this Ordinance.

### 2.2 What are the tests for insolvency in France?

A French company is insolvent (e.g., in a state of cessation of payments (*cessation des paiements*)) if it is not able to meet its payment obligations as and when they fall due for payment with its available assets.

A French company will not be insolvent if it is shown that, because of available assets and/or agreement by any of its creditors to grant additional time to make payment, it can satisfy its liabilities as they fall due from its available assets.

The test of "insolvency" is essentially, therefore, a cash-flow test. It is not a "look forward" test but a test at the time when any payment becomes due and payable. If the company has sufficient assets to pay a debt which becomes due and payable, but does not make payment of that debt, the company will be in default but it will not be insolvent.

### 2.3 On what grounds can the company be placed into each procedure?

Special Mediation is the pre-insolvency proceeding which is most often used when a company in France is undergoing financial or other difficulties. Special Mediation was formally introduced into the restructuring and insolvency legislation in July 2005 but has existed for many years as an emanation of judicial and insolvency practice. In practice, the appointment of a special mediator is used by companies in financial difficulties as a preliminary step to voluntary restructuring. Only the debtor company can request the opening of such proceedings and it must be able to demonstrate that it is solvent at the time.

Conciliation is available to any debtor company which encounters legal, economic or financial difficulties (actual or anticipated) and is solvent or has been insolvent for less than 45 days. Under Conciliation, the company can, with the help of a conciliator appointed by the court, renegotiate its debts with its main creditors. The company will be required to provide details of its financial, economic and social situation including its financing requirements. The conciliator's mission is to seek agreement between the company and its main creditors and the conciliator may be assisted by experts when reporting on the company's economic and financial situation. The conciliation procedure is for a maximum period of five months.

Safeguard may be opened by a debtor company which is solvent, and can demonstrate actual or anticipated difficulties which it cannot overcome. There is no requirement for the debtor company

to demonstrate that the difficulties which it is facing would lead to it becoming insolvent, as was previously the case. Recent case law demonstrates that the French courts will take a wide approach when considering the actual or anticipated difficulties faced by a company.

The Accelerated Safeguard or Accelerated Financial Safeguard may only be initiated by the debtor (or, where it is a corporate body, by its legal representative). However, the opening conditions are quite different from those for Safeguard. The debtor company must already be subject to ongoing Conciliation proceedings, have drafted a plan to ensure the sustainability of its business, have obtained from the creditors affected by the plan sufficiently wide support for the proposed restructuring so as to make the adoption of the plan likely within a maximum period of three months, and either publish consolidated financial accounts or have its accounts certified by a statutory auditor or certified public accountant and meet certain thresholds (in terms of revenues, employees and total net assets) to be set by a decree which has not yet been published.

Importantly, there is no requirement for a company to be solvent if it requests the opening of AS (or AFS) provided it is in Conciliation and was not insolvent for more than 45 days when it initially requested the opening of Conciliation.

Note that from 1 July 2014, the AS will concern all creditors of the company whereas the AFS will still only concern financial creditors. Reorganisation aims to achieve the survival of a company, the preservation of its activities and employment, and the discharge of its liabilities. The court will order the opening of Reorganisation if it can be shown that the debtor is insolvent and has not ceased its activities or if the company is capable of being reorganised. Any debtor in a state of cessation of payments for 45 days must apply to court to start Reorganisation.

Liquidation aims at terminating the debtor company's activities and selling its assets in order to discharge its debts. Liquidation proceedings are opened if the debtor has ceased its activities or is evidently incapable of being reorganised.

### 2.4 Please describe briefly how the company is placed into each procedure.

A request to appoint a special mediator (*mandataire ad hoc*) or conciliator may only be made by the company if the company is solvent. The legal representative of the company (i.e. the board of directors or the president of the board) may formally request the president of the court to appoint an officeholder (referred to as a special mediator). The legal representative of the company can suggest to the court the name of the special mediator or conciliator.

Safeguard may be opened by the court and may only be initiated by the debtor company which is solvent, and can demonstrate actual or anticipated difficulties which it cannot overcome. The debtor is not obliged to prove that the current difficulties it is facing will lead it to cessation of payments. Safeguard is commenced by a court order at the request of the debtor. The public prosecutor may propose the name of the administrator to the court which also has to request the debtor's observations.

Reorganisation must be applied for by the management within 45 days of a company becoming insolvent (unless an application has been made for Conciliation). In addition, a creditor or the public prosecutor may also require the opening of Reorganisation if there is no current Conciliation.

Liquidation may be opened immediately or will be opened where a company is in Reorganisation if it is evidently impossible for the company to be reorganised.

There is a prescribed list of documents and information which needs to be provided to the court with the application for the opening of Safeguard, Accelerated Safeguard, Accelerated Financial Safeguard, Reorganisation or Liquidation, including, for example, information relating to the inventory of assets and liabilities and salaried employees.

Where the debtor company has a works' committees and/or personnel delegates representing salaried employees then there are rules which must be complied with by management prior to the making of an application for the opening of Safeguard or Reorganisation.

Commercial courts in France have been granted wide investigative powers and have many sources of information on the financial or economic situation of private entities and commercial individuals incorporated or registered in their jurisdiction. One of the most important sources of information is the "alert procedure" (*procédure d'alerte*) which can be triggered not only by the statutory auditors but also by the employees' representatives, the shareholders of *sociétés anonymes* (**SA**), partners of *sociétés à responsabilité limitée* (**SARL**) or the president of the court. The alert procedure permits the courts to discover and disclose the financial and economical difficulties of a company and to encourage its managers to take whatever action necessary to address these difficulties.

### 2.5 What notifications, meetings and publications are required after the company has been placed into each procedure?

Special Mediation and Conciliation are confidential proceedings and violation of this confidentiality obligation may give rise to civil liability in damages. Creditors will be notified by the special mediator or conciliator (usually by letter) of the opening of such proceedings and of the special mediator or conciliator's mission and the timing of its mission. As of 1 July 2014, the court decision appointing the special mediator must be communicated to the statutory auditors of the company (if any).

In relation to a Conciliation judgment approved by a commercial court, the judgment approving the Conciliation scheme must be registered by the clerk of the court published in the BODACC and in a legal advertisements journal in the location of the debtor's registered office within eight days from the judgment date.

The judgment opening Safeguard, Reorganisation or Liquidation must be registered with a specific registry depending on the legal status of the debtor. For example, if the debtor is a registered company, the judgment opening the proceedings must be registered with the French trade and commercial registry (*registre du commerce et des sociétés*). The judgment opening the proceedings must also be advertised in two specific journals: the *Bulletin Officiel des Annonces Civiles et Commerciales* (**BODACC**); and in a legal advertisements journal in the location of the debtor's registered office.

The judgment opening an AS or ASF must also be advertised in the BODACC and in a legal advertisements journal in the location of the debtor's registered office.

Creditors (other than employees) must file proofs of claim within two months (four months in the case of certain "foreign" creditors) of the date of publication of the judgment opening Safeguard or Reorganisation in the legal gazette.

The procedure for filing a proof of claim by a creditor upon the opening of the AS or AFS is a simplified proceeding to that of the traditional Safeguard. The debtor company must draw up a list of creditors which have participated in the Conciliation and their

claims will be certified by its statutory auditors or accountants and filed with the court registrar. Recent legislation provides that the *mandataire judiciaire* will be obliged to notify the creditors appearing on this list of the details of their claims by registered letter and not, as was previously the case, by any means. The intention is to better protect the creditors.

As a general rule, there is otherwise no specific individual notification to creditors regarding the opening of formal insolvency proceedings, except for secured creditors who will be notified personally.

The closing judgment, in any of the above proceedings, must also be registered and advertised. The clerk of the competent court must comply with these mandatory requirements within 15 days from the date of the opening or closing judgment.

### 2.6 Are "pre-packaged" sales possible?

Yes. "Pre-packs" are possible in Safeguard, AS, ASF and in Reorganisation. By "pre-pack" we mean a pre-arranged restructuring or reorganisation plan which has been agreed by the requisite majorities of creditors of the debtor company. ASF is now available to holding companies as well as operating companies. Since it is not possible for a debtor company to realise and sell all of its assets and business with Safeguard, any pre-packaged deal involving the sale of assets would likely mean that the debtor company flips into Reorganisation to achieve this.

From 1 July 2014, the preparation of a "pre-pack" may also be possible in Conciliation. At the request of the debtor company and after consultation (*avis*) with the creditors participating in Conciliation proceedings, the conciliator may be empowered to prepare the sale of all or part of the debtor's business which could be implemented later in subsequent Safeguard, Administration or Liquidation proceedings.

## 3 Creditors

### 3.1 Are unsecured creditors free to enforce their rights in each procedure?

In Special Mediation and Conciliation, there is no general stay of creditor rights and remedies as a result of the opening of such proceedings. Depending on the financial difficulties encountered by the debtor company at the time and its ability to meet future payments during these proceedings, the special mediator or conciliator may request (but cannot legally oblige) creditors to suspend payments during the proceedings with a view to ensuring that the debtor company remains solvent throughout the proceedings.

Moreover, pursuant to article 1244-1 of the Civil Code, French courts may, in any civil proceeding involving the debtor, whether initiated by the debtor or the creditor, taking into account the debtor's financial position and the creditor's financial needs, defer or otherwise reschedule the payment dates of payment obligations over a maximum period of two years and decide that any amounts, the payment date of which is thus deferred or rescheduled, will bear interest at a rate which is lower than the contractual rate (but not lower than the legal rate) or that payments made shall first be allocated to repayment of the principal. If a court order under this article is made, it will suspend any pending enforcement measures, and any contractual interest or penalty for late payment will not accrue or be due during the period ordered by the court.

From 1 July 2014, pursuant to article 1244-1 of the Civil Code, the court may impose grace periods of up to two years not only on creditors participating in Conciliation which make a demand for payment or seek to take enforcement action during such proceedings but also on creditors which did not participate in the Conciliation during the performance of a court-approved (*homologué*) or acknowledged (*constaté*) plan. In Safeguard or Reorganisation, and subject to the Financial Collateral Directive, all creditors alike (except for employees), whether secured or unsecured, are prevented from commencing any actions against the insolvent company to obtain any payment for claims which arose prior to the court order initiating the Safeguard or Reorganisation. The stay generally prevents attachments, the enforcement of security, the acceleration of debts, and the termination of contracts on the ground of a payment default and the registration of security interests and preferential rights.

Moreover, the opening of Safeguard or Reorganisation freezes the conclusion or the enforcement of a "*pacte commissoire*" stated in a security agreement.

The opening of Safeguard or Reorganisation suspends and prevents the commencement of legal actions or proceedings against the insolvent company by creditors whose debts arose before the opening of the proceedings and which have as their objective the enforcement of a monetary claim or the termination of a contract on the grounds of a payment default or opening of the relevant Safeguard or Reorganisation themselves.

The opening of Safeguard or Reorganisation suspends all proceedings and any legal process against the insolvent company until the creditor has declared its claim. The proceedings will only be re-initiated, after the administrator, the creditors' representative, or the liquidator are summoned before the court for the sole purpose of confirming the existence and amount of a disputed claim.

There are two exceptions under which unsecured creditors whose claims arose prior to the opening judgment may be paid:

- prior claims relating to salaries which are paid immediately from available monies or, in the absence of funds, by the *Assurance Garantie des Salaires* (**AGS**), within ten days of the judgment opening the applicable proceeding; and
- certain set off payments (see question 3.3 below).

In the case of the Safeguard, this general stay also benefits guarantors of the debtor where the guarantor is an individual during the observation period prior to the court judgment ending the proceedings.

Note that trade suppliers are expressly excluded from the AFS and therefore they can continue to be paid within the time periods contractually agreed.

The opening of Liquidation accelerates claims that were not due and payable.

The opening of Liquidation suspends and prevents the commencement of legal actions or proceedings against the insolvent company by creditors whose debts arose before the opening of the proceedings and which have as their objective the enforcement of a monetary claim or the termination of a contract on the grounds of a payment default.

If it is in the public interest or in the interests of creditors, the court may authorise the continuance of the business for a period not exceeding three months; this period can be extended once for the same period at the request of the public prosecutor. Claims which arise during this period will be treated as preferential claims subject to certain conditions.

The administration of the business is handled by the liquidator or the administrator if he has been appointed. The liquidator may also elect to continue or terminate contracts (this is discussed further below).

The opening of Liquidation accelerates claims that were not due and payable and secured creditors may enforce their security if the liquidator has not proceeded with the Liquidation of the secured assets within a period of three months from the order which commenced the Liquidation.

Only the administrator can elect to carry on with continuing or existing contracts (*contrats en cours*) that are necessary for the continuation of the activities of the company except for small companies (where the debtor can carry on with continuing or existing contracts) (see question 4.4 below).

### 3.2 Can secured creditors enforce their security in each procedure?

In Special Mediation and Conciliation there is no general stay of creditor rights and remedies, including rights to enforce security, as a result of the opening of such proceedings.

In Safeguard or Reorganisation, secured assets do form part of the insolvent estate and enforcement of security interests granted by the debtor company which are, in principle, frozen on the opening of any such proceedings.

Neither the debtor nor the administrator can dispose of the assets of the company without the authorisation of the bankruptcy judge. However, subject to this restriction, the debtor or the administrator may use charged assets as if they were not subject to that charge, save only that any proceeds of sale of the charged assets must be deposited to a special account held by the *Caisse des Dépôts et Consignations*. These sums then cease to be available for the financing of the business during the observation period.

In Safeguard or Reorganisation, the court may order substitution of the secured assets if the parties do not reach an agreement. The insolvency judge may order an advance payment to the secured creditors of all, or part, of their claims. Moreover, the secured creditor's rights of realisation revive if the liquidator has not proceeded with the liquidation of the secured assets within a period of three months from the commencement of compulsory Liquidation.

It appears that creditors with a right of retention (*droit de rétention*), creditors with retention of title clauses (*clause de réserve de propriété*) and creditors to whom the debtor assigned its business debts by way of security under the proceedings of articles L. 313-23 *et seq*. of the Monetary and Financial Code may enforce their rights and are not subject to these proceedings. However, this does not apply to secured creditors under a civil pledge without dispossession, which benefit from a right of retention under article 2286 of the Civil Code but which cannot be enforced during the observation period and the safeguard plan.

The beneficiary of a fiduciary security can, in principle, enforce its security in case of insolvency proceedings (particularly in the case of Liquidation), unless the debtor has the right to use the assets or rights transferred to a fiduciary patrimony pursuant to a use agreement (*convention de mise à disposition*), the fiduciary security cannot be enforced solely as a result of the commencement of Safeguard, the non-payment of debts incurred by the opening of the Safeguard or the adoption by the court of a Safeguard plan.

Proceedings for the recovery of goods (*marchandises*) or movable assets (*biens meubles*) may only be commenced within a three-month period from the publication of the judgment opening the applicable proceedings. Such recovery proceedings can only be commenced if the goods exist "in kind" (en nature) which means that they must still be in the possession of the debtor when the proceeding is initiated and must be clearly identifiable as the goods supplied by the counterparty. The debtor can decide to pay to keep the assets secured by the retention right under authorisation given by the judge or court.

See question 3.3 below for set off rights.

### 3.3 Can creditors set off sums owed by them to the company against amounts owed by the company to them in each procedure?

A creditor who is also a debtor of the insolvent company may have the benefit of a right of set off. Claims are eligible for set off under French law provided that they are certain, can be quantified, and are due prior to the opening of the applicable judgment.

However, a court may allow set off to be effected on the grounds that the debt claims (even if they are not due yet) if it finds that they are legally connected and related (*dettes connexes*). To be considered as related, the debts must be reciprocal or mutual, they must relate to the same agreement, for example the same master agreement, or it must be demonstrated to the court that they are part of one and the same global legal relationship. The creditor will also need to demonstrate that it has filed its proof of claim in good time following the opening of the applicable proceedings.

The implementation of the Financial Collateral Directive in France has been an opportunity to improve the existing French netting legislation by ensuring the enforceability of close-out netting in the event of an insolvency of a French counterparty if certain conditions are met.

As regards claims arising from the operation of the business during the course of the insolvency proceeding, the principle is that such debts must be paid when they become due. Therefore, when both reciprocal debts arise subsequent to the opening judgment, the unpaid creditor is entitled to set off those claims.

## 4 Continuing the Business

### 4.1 Who controls the company in each procedure? In particular, please describe briefly the effect of the procedures on directors and shareholders.

In the case of Special Mediation, the management of the company remains in the hands of the chairman and the board; in practice they are likely to follow the recommendations of the special mediator. Special Mediation is not coercive, but in the event that the special mediator's mission does not lead to an agreement between the company and its main creditors, there is likely to be a real risk of insolvency proceedings being opened in respect of the company.

In the case of Conciliation, the management of the company also remains in the hands of the chairman and the board. Management will consult with the conciliator as a matter of practice.

In Safeguard, the debtor retains management control of the company. The court may, however, appoint one or several administrators (*administrateurs judiciaires*) and may entrust him/them (as officers of the court) jointly or individually with the duty of supervising the debtor in the management of its business or assisting the debtor in whole or in part in relation to its management acts.

In Accelerated Safeguard and Accelerated Financial Safeguard, the debtor also retains management control of the company. The court

will often appoint the conciliator in the previous Conciliation as administrator. However, the court may appoint another person as administrator but must give specific reasons for this decision. The role of the administrator is to supervise or assist the debtor in reaching the final approval of the plan prepared during the Conciliation. As in Safeguard, a creditor's representative (*mandataire judiciaire*) is also appointed by the court.

In Reorganisation, the debtor company is, in principle, entitled to remain in charge of the management of that part of its business that has not been transferred to the administrator by the court's decision or that has not been taken over by the administrator pursuant to the terms of the insolvency law. The court, however, may appoint an administrator to assist (rather than only to supervise as in the case of Safeguard) the debtor in the management of its business. In contrast to Safeguard, the court can also require the administrator to take over, in whole or in part, the management of the business.

In Reorganisation only, the acts of management that the debtor is entitled to undertake in the ordinary course of its business are subject to prohibitions concerning the entry into certain transactions (such as transactions at an undervalue, preferences, termination of contracts, and payment of debts arising before the opening of the Reorganisation). The court can also appoint one or more experts for specific purposes if it is deemed necessary.

When Safeguard or Reorganisation relate to small companies, the court has no obligation to appoint an administrator. In that case, the debtor is allowed to carry on the business alone. Nevertheless, the court may, at the request of the debtor, the creditor's representative, or the public prosecutor, appoint an administrator. When an administrator is appointed by the court to take over the sole management of the business of the debtor, the court must appoint one or more experts to assist the administrator in his duties.

When opening compulsory Liquidation, either immediately or at the end of the observation period, the court will appoint a liquidator who takes control of the company and is in charge of collecting, realising and liquidating the assets of the company. Unlike Safeguard or Reorganisation, the debtor is immediately and automatically discharged from the management of the company and all of its assets.

In each of the above cases, shareholders continue to exercise their shareholder rights. In Reorganisation, the court may impose restrictions on the ability of de jure and de facto managers of the company (including majority shareholders) to sell their equity interests in certain cases but generally shareholders cannot be compelled to provide new money or accept a debt for equity swap in any restructuring.

### 4.2 How does the company finance these procedures?

This is not applicable for Special Mediation and Conciliation except that, from 1 July 2014, any contractual provision which provides that the fees of any advisor to a creditor will be borne by the debtor solely as a result of the appointment of a *mandataire ad hoc* or a conciliator or the opening of *Mandat ad hoc* or Conciliation (over and above a percentage amount to be fixed by *arrêté*) shall be deemed to be null and void (*non écrite*).

Effectively, during the applicable observation period in Safeguard or Reorganisation, finance results are legally connected from the general stay on the payment of pre-opening judgment claims, available cash in bank accounts existing at the date of the opening judgment, and trade receivables received during the observation period.

Where new money is made available during the observation period in Safeguard to meet expenses incurred during that period, such amounts will benefit from special priority of repayment terms at the end of the observation period.

The expenses and fees of the administrator and liquidator and court fees are also paid on a priority basis.

### 4.3 What is the effect of each procedure on employees?

Statutory amounts due to salaried employees prior to the judgment opening the applicable proceedings are paid within 10 days of that opening judgment. If the debtor company does not have sufficient funds available at that time to meet such payments, these are paid from the first available proceeds received by the debtor company. Further, if there are sufficient funds, an amount equal to one month of unpaid salary is to be paid to the employees and following the opening judgment, such amounts are paid as they become due.

Salaried employees also benefit from a guarantee from the French state fund (*Assurance Garantie des Salaires*) during both Safeguard and Reorganisation.

If it is necessary to terminate employees' employment contracts, then this will be effected under Safeguard in accordance with general French labour law provisions and in Reorganisation or Liquidation pursuant to a more simplified procedure.

### 4.4 What effect does the commencement of any procedure have on contracts with the company and can the company terminate contracts during each procedure?

This is not applicable for Special Mediation or Conciliation except that, from 1 July 2014, any contractual provision which modifies performance of a contract "in progress" (*contrat en cours*) by reducing the rights of a debtor or increasing its obligations solely as a result of the appointment of a *mandataire ad hoc* or conciliator or opening of *Mandat ad hoc* or Conciliation will be deemed to be null and void (*non écrite*). As a matter of case law, contracts "in progress" (*contrat en cours*) are defined under French insolvency laws as "all contracts whose principal obligations have not been performed at the time of the insolvency judgment".

The opening of Safeguard or Reorganisation does not automatically terminate contracts or extinguish rights. Following his assessment of the debtor's interests, only the administrator may elect to continue contracts "in progress" (*contrats en cours*). Therefore, a contract cannot provide for its termination (either automatically or on the giving of notice) only by reason of insolvency.

Upon the opening of Safeguard or Reorganisation, counterparties of the debtor company are entitled to send a formal notice inviting the administrator to exercise his option to continue contracts to which the company is party. The contract will be deemed terminated if the administrator does not respond to this formal invitation within one month. The bankruptcy judge may require the administrator to respond within a shorter period or may extend the period in which the administrator must make his decision, but for no longer than two months. The administrator can ask the bankruptcy judge (*juge commissaire*) to order the termination of contracts to protect the company's business and when such termination does not undermine his contracting partner's interests.

The administrator must, when he elects to continue a contract, check whether the company has, or will have, the funds to perform its obligations. He may only elect to continue an existing contract if the company is able to perform its obligations under the contract

(i.e., any payments, and the performance of any obligations, under the contract must be made in accordance with its terms and conditions). If the administrator chooses to continue the contract and it subsequently appears that the company is not in a position to perform its obligations under the contract, or if the company fails to perform its obligations, the counterparty recovers its right to terminate the contract pursuant to its provisions.

In the case of leases, the right of a landlord to terminate the lease of property used in the business of the company is restricted in insolvency proceedings. The landlord can only terminate a lease of property (or obtain an acknowledgment of the termination of the lease) following a lease payment default relating to lease occupation after the judgment opening the proceedings. Whether there has been a lease payment default will be assessed at the end of a three-month period from the date of the judgment opening the proceedings. Moreover, the default of occupation during the observation period will not terminate the lease contract.

In the case of a contract which has been wholly performed by the solvent counterparty, but where there are still obligations to be performed by the insolvent company, the debtor or the administrator is unlikely to cause the insolvent company to perform its obligations and the solvent counterparty will generally be left with an unsecured claim for damages in this respect.

Fiduciary agreements (*contrats de fiducie*) are not subject to these rules; however, if the goods or rights included in the trust property have been left at the debtor's disposal pursuant to an agreement (*contrat de mise à disposition des biens*), this agreement will be subject to continuance and termination rules of contracts.

## 5 Claims

### 5.1 Broadly, how do creditors claim amounts owed to them in each procedure?

This is not applicable for Special Mediation or Conciliation.

From the date of the official publication of the opening of Safeguard or Reorganisation, all creditors whose claims have arisen before this order (with the exception of employees) must file a proof of claim with the creditors' representative (or with the liquidator). Creditors whose security has been officially registered will be notified personally that they have to file a proof of claim. Claims that have arisen after the order commencing insolvency proceedings and which do not meet the requirements to be considered as preferential debts, must also be declared.

The proof of claim must be made even if the title to the claim has not been established. The proof of claim sets out the total amount claimed as at the date of the opening of the insolvency proceedings, including any amount falling due in the future, together with the dates on which the claims fall due. The proof of claim must set out the nature of any preferential right or security attached to a claim. Subject to limited exceptions, the creditor must certify that the claim is fair and correct. The bankruptcy judge may require the statutory auditors or the accountants of the creditor to certify the declaration of claim.

Each creditor must file its proof of claim within two months (or four months for creditors not incorporated in France), otherwise it will not be entitled to share in distributions and dividends. The non-declaration of claims within the specified time limit will not affect the existence of the debt itself but will prevent the creditor from asserting his creditor rights against the debtor (and the guarantor if it is an individual) during the safeguard scheme approved by the court. The creditor who has not duly filed a proof of claim will also definitely lose the right to enforce it against the debtor in the event that the debtor in due course fully complies with the safeguard scheme approved by the court.

In AS or ASF, the same rules exist for the filing of proofs of claim by creditors as for Safeguard. However, for creditors who participated in the Conciliation entered into as a prerequisite of the opening of ASF, a list of debts at the date of the opening judgment of the ASF is established by the debtor and certified by the statutory auditor or, by default, by a chartered accountant (*expert-comptable*). This list of debts is given to the clerk of the competent court. The creditor's representative informs each concerned creditor about the characteristics of the debts mentioned in the list. The debts included in the above list are deemed as having been registered, subject to any objections from creditors.

### 5.2 What is the ranking of claims in each procedure? In particular, do any specific types of claim have preferential status?

This is not applicable generally for Special Mediation or Conciliation.

In Conciliation, new money providers who make credit available within the terms of the court approved arrangements (*homologation*) and prior to it during the Conciliation proceedings itself for the purposes of ensuring the continuation of the company's business during the conciliation period will have priority over claims of creditors (other than super-priority salary claims and court fees and expenses) which arose prior to the date of the opening of the Conciliation if the company is subsequently placed into Safeguard, Reorganisation or Liquidation. Similar provisions also apply to suppliers of new services or assets for such purposes. These provisions do not apply to shareholders making contributions in respect of share capital increases.

The rules relating to the ranking of claims in Safeguard, Reorganisation and Liquidation for pre- and post-opening judgment claims are complex.

Claims will generally be paid in accordance with a statutory order of priority involving super-priority salary claims, then court costs and expenses and those related to the applicable proceedings, new money claims arising after the order commencing insolvency proceedings was made but which are incurred for the purpose of administering the applicable insolvency proceedings during the observation period, certain other preferential claims, then secured and unsecured claims. Some claims may be secured or subordinated contractually or by statute.

### 5.3 Are tax liabilities incurred during each procedure?

Yes, but the French public authorities may grant debt forgiveness (but not for indirect taxes other than penalties and late interest). Three enabling decrees have been implemented in relation to the debt forgiveness which public authorities may grant to ensure that competition is not falsified by such debt forgiveness and that the European Commission does not consider such debt forgiveness as state aid. Public authority debt forgiveness must be carried out in the same manner as the private sector would have agreed in relation to the reduction of debt in the ordinary course of the market. Such public debt forgiveness will be subject to a ceiling. The level of this ceiling will depend on the amount of debt reduction given by private creditors (with the exception of inter-company debt reduction). A specific procedure must be followed in relation to public debt forgiveness. Generally, the public authorities, rather than writing off debt, prefer to extend the time period in which the debtor will have to pay the relevant public debts.

## 6 Ending the Formal Procedure

### 6.1 What happens at the end of each procedure?

In the case of Special Mediation, if a restructuring agreement has been found between the company and its creditors, the proceedings will terminate. If new money is required or there is some doubt as to the debtor company's solvency for the purposes of implementing the restructuring, the Special Mediation may be converted into Conciliation in order to obtain a court approval of the new money arrangements and other advantages attached to this judgment.

Safeguard comes to an end either with the adoption of a safeguard plan to be implemented by the debtor company, or, in case of an intervening insolvency during the Safeguard, with the opening of Reorganisation or Liquidation. The opening of Liquidation is mandatory if cessation of payments intervenes during the implementation of the Safeguard Plan. The Safeguard may also be closed on request by the debtor company when the difficulties which caused its opening cease to exist.

Reorganisation comes to an end either with: the adoption of a continuation plan to be implemented by the debtor company under the supervision of a court-appointed trustee (*commissaire à l'exécution du plan*); or the adoption of a sale and transfer plan by which all or part of the business sold; or by conversion into Liquidation. The proceeding may also be closed if the insolvency no longer exists.

## 7 Restructuring

### 7.1 Is a formal procedure available to achieve a restructuring of the company's debts in France?

Yes. In the absence of any consensual restructuring within the Special Mediation, a restructuring of the company's debts may be made within the Conciliation, Safeguard, AS, ASF or Reorganisation proceedings. As mentioned above, Conciliation remains a consensual restructuring procedure where the Conciliation plan may be formally approved by the French court with a view to obtaining a new money privilege for example. Safeguard, AS, ASF and Reorganisation proceedings may be used to extend the repayment of a debtor company's financial indebtedness or subject to applicable majority consents by creditors' committees, to more fundamentally restructure the company's debt.

From 1 July 2014, any member of a creditors' committee in Safeguard or Administration will also be able to submit a draft plan to the administrator who will submit plans received from the debtor and any creditors to the vote of the creditors' committees. Since bondholders are not members of a "creditors' committee" it does not appear that bondholders will be able to submit their own draft restructuring plan.

### 7.2 If such a procedure is available, is a debt for equity swap possible and how are existing shareholders dealt with?

It is not uncommon to see a debt for equity swap as part of the French consensual restructuring plan among all stakeholders. However, a debt for equity swap will require the consent of the shareholders and there is no formal mechanism to oblige the shareholders to agree to a debt for equity swap.

From 1 July 2014, an administrator may request the court to empower a *mandataire* to call a shareholders' meeting and to vote on the reconstitution of a company's share capital in the minimum amount required by law if the company has lost more than half of its share capital and a shareholder refuses to participate in the reconstitution of the company's share capital.

Note that the draft Ordinance of those published on 12 March 2014 contained a provision which would have allowed the sale of a controlling shareholders' shares in administration if so ordered by the court. This has not been retained in the published Ordinance. We understand that this provision, which practitioners were very much in favour of, is under review by the French Chancellery and may be introduced at a later stage (by the summer of 2014), although there is no certainty that this will be the case.

### 7.3 Can dissenting creditors be crammed down?

This is not applicable for Special Mediation or Conciliation.

Yes, in the case of the Accelerated Safeguard or Accelerated Financial Safeguard. Only financial creditors are affected by the opening of the ASF and will be consulted on the draft plan after the constitution of a financial institution's creditors' committee whereas all creditors of the company may be affected by the AS. Bondholders will also be consulted and will have their own meeting to consider the plan. However, trade creditors are expressly excluded from this procedure and will be paid within the time period contractually agreed.

The financial institution's creditors' committee and, where applicable, the bondholders' assembly are invited to vote on the draft plan already prepared during the Conciliation procedure (the pre-packed plan) within a period of 20 to 30 days from the receipt of the debtor's proposal (the bankruptcy judge may extend or reduce this period of time without making it shorter than fifteen days in an AS or eight days in an AFS).

The plan must be approved by the court within three month from the opening of the AS. In an AFS, this delay is reduced to one month (with a possible extension of one month). The voting requirements for approving the draft plan are the same as for the regular Safeguard. The decision is taken by a two-thirds majority of debt claims held by members of that committee who have voted on the debtor's proposals. In certain circumstances, the draft plan must also be approved by a two-thirds majority of the aggregate amount of bond claims held by bondholders. If the credit institution's creditors' committee and, where applicable, the bondholders' general meeting, do not approve the plan within the period mentioned above (and there has been no extension of this time period), the court will terminate the procedure.

Yes, in main Safeguard or Reorganisation, where the Safeguard plan is approved by the relevant committee and, where applicable, by the general meeting of bondholders, this will bind all members of the committee if the Safeguard plan is then approved by the court. In addition to considering whether there is a serious possibility of the company continuing its business, the court must take into account whether the interests of other creditors are sufficiently protected in deciding whether or not to approve the proposed Safeguard plan.

The court-approved Safeguard plan will not be binding on creditors who are not members of the committees unless they have agreed to its terms but the court can reschedule repayment of their debts over a maximum period of 10 years, except for debts with maturity dates of more than 10 years, in which case the maturity date may remain the same.

For companies with more than 150 employees or a turnover of up to EUR 20 million and whose accounts are certified by a statutory auditor (*commissaire aux comptes*) or upon request of the debtor or the administrator, two committees of creditors must be established following the order opening the Safeguard (this rule also applies to Reorganisation). However, the bankruptcy judge may authorise the constitution of creditors' committees for companies which do not meet the thresholds at the debtor's or the administrator's request.

The financial creditors' committee comprises financial institutions as well as similar entities and any entity with which the debtor concluded any credit agreement, and the second comprises of trade suppliers. The threshold to be a member of the suppliers' committee was lowered to the holding of 3 per cent of the total suppliers' debts.

The committees' membership is determined by reference to the claims which have arisen before the date of the opening of the proceedings. The selection of committee members is carried out by taking into account the aggregate amount of outstanding debts as certified by the statutory auditors. The mandatory or optional attendance at creditors' committees is considered to be attached to the claim itself. Accordingly, taking part in such committees constitutes an accessory of the claim, transferred automatically to the successive holders of the claim regardless of any provisions to the contrary. Thus the transferee of bank claims against the debtor will become a member of the financial committee even if the claims transfer is implemented after the judgment opening the insolvency proceedings. Local communities (*collectivités territoriales*) and public establishments (*établissements publics*) are not members of the suppliers' committee.

Bondholders are not members of the financial institutions' committee. Bondholders are gathered in a single meeting comprising all creditors' holding bonds, whatever their type or the countries where they were issued and irrespective of the terms of those bonds. The administrator convenes a meeting of bondholders to vote in the bondholders' assembly on the scheme proposal which has been previously adopted by the two creditors' committees.

Creditors who are not affected by the draft plan (i.e., there will be no modification of their payment terms) or who will be paid in whole in cash (in accordance with the draft plan or when their debts are admitted) will not vote on the plan. Creditors may be treated differently (i.e., not equally) if the situation so justifies.

Creditors who are not members of the committees and creditors benefiting from a trust (for part of their secured claims) are consulted individually by the administrator on the proposed debt settlement.

When: (i) one of the two committees does not agree to the proposed Safeguard scheme within the deadline; (ii) one of the two committees rejects the proposed scheme; (iii) the bondholders do not agree to the proposed Safeguard scheme within the deadline; (iv) the bondholders reject the proposed scheme; (v) the court does not approve the proposed Safeguard scheme; or (vi) the debtor does not make any proposals within the deadline, the process for approving the Safeguard scheme will generally follow the one described above for creditors who are not members of either committee.

### 7.4 Is consent needed from other stakeholders for a restructuring?

See question 7.2 (above) in respect of a formal restructuring process.

## 8 International

### 8.1 What would be the approach in France to recognising a procedure started in another jurisdiction?

Insolvency proceedings commenced in respect of companies having their "centre of main interests" within the boundaries of the European Union are now dealt with by the Regulation. The Regulation applies to any commercial or industrial business and to individuals carrying out business activities (such as artisans), but does not apply to groups of companies, insurance companies, or collective investment undertakings.

Under the Regulation, courts of the Member State within the territory of which the centre of a debtor's main interests is situated have jurisdiction to open insolvency proceedings. The law applicable to these proceedings is the law of the Member State in which proceedings are opened, subject to limited exceptions. The decision opening insolvency proceedings in one Member State is immediately recognised in all other Member States and is effective in all other Member States. The appointed liquidator has very wide powers on the debtor's assets that are situated in other Member States.

Secondary proceedings can be opened in other Member States but main proceedings will prevail over secondary proceedings. In France this procedure could only be introduced as a Liquidation governed by French law. The Regulation also provides for a duty to co-operate and to communicate information between the liquidator in the main proceedings and the liquidator in the secondary proceedings.

French courts therefore recognise and apply the Regulation. The only exception to this recognition would be if the applicable decision is contrary to French public order.

France has entered into some international treaties with other countries in relation to insolvency proceedings (e.g., Belgium, Italy and Austria). These treaties will continue to apply to issues not covered by the Regulation.

Finally, as regards recognition of insolvency-related procedures and judgments opened outside the EU, a procedure known as "*exequatur*" would need to be undertaken before the French courts in order to seek to obtain recognition.

**Rod Cork**

Allen & Overy LLP
52 avenue Hoche
CS 90005
75379 Paris Cedex 08
France

*Tel:* *+33 1 4006 5570*
*Fax:* *+33 1 4006 5454*
*Email:* *rod.cork@allenovery.com*
*URL:* *www.allenovery.com*

Rod Cork is a partner within the Banking department of Allen & Overy LLP Paris where he has been based for over twenty years. Rod has a wide experience advising on general banking matters, including acquisition and corporate finance and restructurings. He has acted for lenders on a wide range of public and private corporate restructurings in France, Europe and North America. He has also acted on a number of restructurings of French LBOs and property and structured finance transactions. Rod is qualified as an English solicitor and is also a member of the Paris Bar.

**Marc Santoni**

SCP Santoni & Associés
15 avenue d'Eylau
75116 Paris
France

*Tel:* *+33 1 4405 1111*
*Fax:* *+33 1 4405 1441*
*Email:* *msantoni@scp-santoni.com*
*URL:* *www.scp-santoni.com*

Founder of the law firm SCP Santoni & Associés 20 years ago, Marc's activity has since then been devoted to the management of French businesses in difficulty and to investment funds advisory.
Marc advises buyers interested in companies' turnaround as well as companies under special mediation ("*mandat ad hoc*") or safeguard-rehabilitation-liquidation proceedings ("*sauvegarde-redressement-liquidation judiciaire*"). He intervenes in the treatment of underperforming LBO on behalf of many investment funds.
Marc is President of the "*Association des Avocats de la Prévention et des Procédures Collectives (A2PC)*". He is also a member of the "*Association pour le Retournement des Entreprises*" (Association dedicated to companies survival and turnaround) and of the "Turnaround Management Association" (TMA), and takes part in investment boards of many investment funds.

ALLEN & OVERY

Allen & Overy LLP offers a wide range of services to international and domestic restructurings, with a dual expertise in corporate and banking laws. Allen & Overy and leading French law insolvency practice Santoni & Associés have a strategic arrangement and work together on restructuring and insolvency related work in France. This arrangement covers all types of debt restructurings and work-outs, corporate and fund buy-outs, refinancings, pre- and post-insolvency related procedures and distressed debt trades in France.

The arrangement is the fruit of a close collaboration between Allen & Overy and Santoni & Associés over many years on restructuring and insolvency related matters in France. It enables the two firms to pool their expertise and resources on domestic and international cross-border transactions covering both public and private companies, LBOs and structured transactions.