INSOL INTERNATIONAL

FOUNDATION CERTIFICATE IN INTERNATIONAL INSOLVENCY LAW

Module 6A Guidance Text

France

2023 / 2024

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Published: September 2023

1. INTRODUCTION TO INTERNATIONAL INSOLVENCY LAW IN FRANCE

Welcome to **Module 6A**, dealing with international insolvency law in **France**. This Module is one of the elective module choices for the Foundation Certificate. The purpose of this guidance text is to provide:

- a general overview, including the background and history, of insolvency law in France;
- a relatively detailed overview of France's insolvency system, dealing with both corporate and consumer insolvency; and
- a relatively detailed overview of the rules relating to international insolvency and how they are dealt with in the context of France.

This guidance text is all that is required to be consulted for the completion of the assessment for this module. You are not required to look beyond the guidance text for the answers to the assessment questions, although bonus marks will be awarded if you do refer to materials beyond this guidance text when submitting your assessment.

Please note that the formal assessment for this module must be submitted by **11 pm (23:00) BST (GMT +1) on 31 July 2024**. Please consult the Foundation Certificate in International Insolvency Law web pages for both the assessment and the instructions for submitting the assessment. Please note that no extensions for the submission of assessments beyond 31 July 2024 will be considered.

For general guidance on what is expected of you on the course generally, and more specifically in respect of each module, please consult the course handbook which you will find on the web pages for the Foundation Certificate in International Insolvency Law.

2. AIMS AND OUTCOMES OF THIS MODULE

After having completed this module you should have a good understanding of the following aspects of insolvency law in France:

- the background and historical development of insolvency law in France;
- the various pieces of primary and secondary legislation governing French insolvency law;
- the operation of the primary legislation in regard to liquidation and corporate rescue;
- the operation of the primary and other legislation in regard to corporate debtors;
- the rules of international insolvency law as they apply in France;
- the rules relating to the recognition of foreign judgments in France.

After having completed this module you should be able to:

- answer direct and multiple-choice type questions relating to the content of this module;
- be able to write an essay on any aspect of French insolvency law; and
- be able to answer questions based on a set of facts relating to French insolvency law.

Throughout the guidance text you will find a number of self-assessment questions. These are designed to assist you in ensuring that you understand the work being covered as you progress through text. In order to assist you further, the suggested answers to the self-assessment questions are provided to you in **Appendix A**.

3. AN INTRODUCTION TO FRANCE

France lies near the western end of the great Eurasian landmass. It is a transcontinental country, spanning Western Europe and overseas regions and territories in the Americas and the Atlantic, Pacific and Indian Oceans. Its metropolitan area extends from the Rhine River (in the east) to the Atlantic Ocean (in the west); and from the Mediterranean Sea (in the south) to the English Channel and the North Sea (in the north); and as a result, France has long provided a geographic, economic and linguistic bridge joining northern and southern Europe. In 2021, its population was estimated at 65,404,000. France is the most visited country in the world, with an all-time high total of 89.4 million foreign tourists in 2018.

France has been influential in governmental and civil affairs, providing the world with important democratic ideals in the age of the Enlightenment and the French Revolution, and inspiring the growth of reformist and even revolutionary movements for generations. The present Fifth Republic has enjoyed notable stability since its promulgation in 1958, marked by important growth in private initiative and the rise of centrist politics. Although France has engaged in long-running disputes with other European powers, it emerged as a leading member of the European Union (EU), of which it is also a founding member.

From 1966 to 1995 France did not participate in the integrated military structure of the North Atlantic Treaty Organization (NATO), retaining full control over its own air, ground, and naval forces. From 1995, however, France was represented on the NATO Military Committee, and in 2009, French President Nicolas Sarkozy announced that the country would re-join the organisation's military command. As one of the five permanent members of the United Nations Security Council, France has the right to veto decisions put to the council.

With a total population of around 64 million people, France is one of the major economic powers of the world. While in the 1950s agriculture and industry were the dominant sectors, tertiary (largely service and administrative) activities have since become the principal employer and generator of national wealth. Despite the dominance of the private sector, the tradition of a mixed economy in France is well-established. Successive governments have intervened to protect or promote different types of economic activity, as has been clearly reflected in the country's national plans and nationalised industries. While the government has partially or fully

privatised many large companies, including Air France, France Telecom, Renault and Thales, it maintains a strong presence in some sectors, particularly power, public transport and defence industries.

Workers' incomes are taxed at a high to moderate rate, and indirect taxation in the form of a value-added tax (VAT) is relatively high. Overall, taxes and social security contributions levied on employers and employees in France are higher than in many other European countries.

France has one of the largest banking sectors in western Europe, and its three major institutions, Credit Agricole, BNP Paribas and Société Générale, rank among the top banks on the continent. France also has a large insurance industry dominated by major companies such as Axa, CNP and AGF, but also including a number of important mutual benefit societies, which administer pension plans.

France, a leading trading nation, has grown into one of the world's foremost exporting countries, with the value of exports representing more than one-fifth of the gross domestic product (GDP). France is also a major importer of especially machinery, chemicals and chemical products, tropical agricultural products and traditional industrial goods such as clothes and textiles. France has become an increasingly important net exporter of raw agricultural products (such as grains) as well as agro-industrial products, such as foods and beverages, including wines, tinned fruits and vegetables and dairy products. It is also a major exporter of vehicles and transport equipment, as well as armaments and professional electronics.

The greater part of foreign trade is carried out with other developed countries and four-fifths of transactions take place with countries that are members of the Organisation for Economic Co-operation and Development (OECD). The EU plays a major role in foreign trade, with more than three-fifths of French exports and imports destined for, or originating in, EU member states. Outside the EU, the United States (US) is France's other major trading partner, although Russia and China have claimed a growing percentage of French trade in the 21st century.

France's real GDP grew by 1.8% in 2019, with a GDP per capita of US$41,990. However, unemployment remains a rampant issue for the French economy, stagnating year over year since the financial crisis of the late 2000s. During the first quarter of 2018, more than 1.4 million people aged between 25 and 49 years were unemployed in France. France's public finances have historically been constrained by high spending and low growth. In 2017, the budget deficit improved to 2.7% of GDP, bringing it in compliance with the EU-mandated 2% deficit target. Meanwhile, France's public debt rose from 89.5% of GDP in 2012 to 97% in 2017.

France has a mixed, semi-presidential form of government, combining elements of both parliamentary and presidential systems. The Parliament is a bicameral legislature composed of elected members of the National Assembly (lower house) and the Senate (upper house). The president is elected separately by direct universal suffrage and operates as head of state. The constitution gives the president the power to appoint the prime minister, who oversees the execution of legislation. The president also appoints the Council of Ministers, or cabinet, which together with the prime minister, is referred to as the government.

France is a civil law system, which means that it derives from statutes and written laws, which are generally organised in codes (for example, the Civil Code, the Criminal Code, the Commercial Code, the Labour Code, etcetera). Judges strictly apply these laws in order to avoid legal uncertainty and prevent arbitrary or excessive legal decisions. Jurisprudence is therefore not considered an autonomous source of law but rather exists as a consequence of codified laws, as the tendency is to judge in a certain way in similar situations.

4. LEGAL SYSTEM AND INSTITUTIONAL FRAMEWORK

4.1 Legal system

French insolvency law has a long and ancient history, dating back to Roman law. Before the introduction of the Commercial Code of 1807, insolvency law was mostly of a coercive nature, with procedures consisting of arresting and imprisoning the defaulting debtor. Even with the promulgation of the Commercial Code of 1807, French bankruptcy law still severely punished bankrupt debtors as the bankruptcy procedure in place consisted of arresting and imprisoning defaulting persons and selling their assets in order to pay back their debts.

Even though the Law of 4 March 1880 introduced the liquidation procedure (which ran alongside the coercive bankruptcy procedure for honest bankrupt debtors who could save their businesses through debt forgiveness from their creditors), the roots of modern insolvency law can be traced back to the 1950s[1] and the 1960s.[2] During this time the corporate insolvency landscape was transformed considerably and the first rescue procedure was introduced (*redressement judiciaire*).

The Law of 13 July 1967 considerably transformed the insolvency landscape by dissociating the fate of the company from that of its management. In doing so, a “twin-track” system was established, whereby a company could either be liquidated or rescued. The first pre-insolvency process was introduced as early as 1984.[3]

The year 2000 marked the promulgation of the new Commercial Code that consolidated insolvency laws as part of the bicentenary celebrations of the great codification project inaugurated by Napoleon I. Since then, the French legislator and government have been prolific at updating the insolvency regime at regular intervals, with substantial reforms taking place every couple of years.

This continuous reform activity has partly been as a result of regular economic crises, which have led to an increase in the number of insolvency cases, and partly due to the consideration that previous reforms had fallen short of success. Most reforms have centred around the acknowledgment that corporate difficulties should be dealt with upstream, in order to preserve the value of the assets of the company and to facilitate a successful restructuring.

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1 Decree-Law No 55-583 of 20 July 1955.
2 Law No 67-563 of 13 July 1967.
3 Law No 84-148 of 1 March 1984.

In 2005, the safeguard procedure (*procédure de sauvegarde*) was instituted, introducing a debtor-in-possession process into French insolvency law. It was designed to encourage upstream rescue, since companies can benefit from it before becoming officially insolvent. In 2008, following a rather low take-up of the procedure, the government attempted to address its main flaws.[4] In the wake of the global economic and financial crisis of the late 2000s, variations of the safeguard procedure were created: the accelerated financial safeguard (*sauvegarde financière accélérée*) in 2010[5] and the accelerated safeguard (*sauvegarde accélérée*) in 2014,[6] which drew on the practice of pre-packs.

French insolvency law was once again reformed in 2014, with the aim to:

(1) promote preventive measures;

(2) strengthen the efficiency of pre-insolvency proceedings; and

(3) increase the rights of creditors in insolvency proceedings.[7]

In 2016, the Law on the Modernisation of 21st Century Justice focused on the promotion of the rescue culture, the enhancement of confidentiality during proceedings, the ring-fencing of new monies during restructuring and the improvement of transparency and impartiality.[8]

In 2019, the French legislator passed the so-called *Pacte* Law (*Plan d'Action pour la Croissance et la Transformation des Entreprises*).[9] This law is one of the latest steps in the economic strategy of the country and has two main objectives:

(1) business growth and job creation; and

(2) the redefinition of the place of a company in society with a view to better involving employees in the existence of a company.[10]

In order to achieve these, the *Pacte* Law tasked the French government with transposing the provisions of the EU Directive on Preventive Restructuring by means of an ordinance. The latter became effective in September 2021.[11]

France is therefore now equipped with a comprehensive body of insolvency procedures, all governed by Title VI of the Commercial Code (*Code de Commerce*). In addition to liquidation proceedings, French insolvency law proposes a vast array of restructuring procedures, which

4 Ordinance No 2008-1345 of 18 December 2008.
5 Law No 2010-1249 of 22 October 2010. The accelerated financial safeguard has now been merged within the accelerated safeguard procedure.
6 Ordinance No 2014-326 of 12 March 2014.
7 *Ibid*.
8 Law No 2016-1547 of 18 November 2016.
9 Law No 2019-486 of 22 May 2019.
10 See the Report of the French Council of Ministers of 18 June 2018. Available at https://www.gouvernement.fr/conseil-des-ministres/2018-06-18/croissance-et-transformation-des-entreprises.
11 Ordinance No 2021-1193 of 15 September 2021.

explains why France is internationally known as a "restructuring-biased" jurisdiction[12] that is predominantly geared towards the rescue of ailing businesses, with a view to preserving employment.

The current corporate insolvency law system is comprised of the following procedures:

(1) *Ad hoc* mandate (*mandat ad hoc*);

(2) Conciliation;

(3) Safeguard (*sauvegarde*) ;

(4) Accelerated safeguard (*sauvegarde accélérée*);

(5) Judicial rehabilitation (*redressement judiciaire*);

(6) Liquidation; and

(7) Bankruptcy.

4.2 Institutional framework

4.2.1 General framework

Generally, the French judicial system is divided into two orders or court systems, namely a judicial order (*ordre judiciaire*) and an administrative order (*ordre administrative*). These two orders are independent and autonomous and they operate within their own hierarchical structures. Each has its own supreme court at the top of its hierarchy: the *Cour de Cassation* for the judicial order and the *Conseil d'Etat* for the administrative order. The judicial courts handle criminal, civil, commercial and labour law cases, which are collectively referred to as private law, while the administrative courts handle all public law matters involving national or local governments, including matters between citizens and public authorities.

The judicial order is further divided into:

(a) Courts of first instance and of general jurisdiction, which are further divided into:

- criminal courts (*tribunal de police*: dealing with minor offences; *tribunal correctionnel*: dealing with misdemeanours such as theft; and *court d'assises* (Crown court): dealing with serious criminal cases, such as rape or murder); and

- civil courts (*tribunal judiciaire*: dealing with any claim for which a specialised court is not required).

[12] M Adalet McGowan and D Andrews, "Insolvency Regimes And Productivity Growth: A Framework For Analysis", *OECD Economic Department Working Papers No 1309* (2016) at 18.

(b) Specialised courts of first instance, such as:

- labour courts (*conseil de prud'hommes*);
- social security courts (*tribunal des affaires de la sécurité sociale*); and
- commercial courts (*tribunal de commerce*).

The Court of Appeal (*Court d'appel*) has jurisdiction over appeals from all courts of first instance. The highest judicial body in France is the Supreme Court (*Cour de cassation*).

4.2.2 *The insolvency framework*

It should firstly be noted that there is no insolvency regulator in France. Rather, insolvency law and cases are governed by the Commercial Code, the courts and specific insolvency stakeholders.

Secondly it should be noted that the courts that have jurisdiction over insolvency proceedings will differ depending on the nature of the debtor and the type of activity carried out: (i) the commercial court if the debtor carries out a commercial or agricultural activity; or (ii) the judicial court if the debtor carries out an "independent profession"[13] (*profession libérale*).

In some specific cases, the specialised commercial court (*tribunal commercial spécialisé*) can also be competent. This would be the case where the debtor carries out a commercial or agricultural activity and if the debtor is a company:

- whose employees exceed 250 and turnover exceeds EUR 20 million; or
- whose turnover exceeds EUR 40 million; or
- that holds or controls other entities, where the total combined number of employees is 250 or above and where the combined total turnover is of at least EUR 20 million; or
- that holds or controls other entities and where the combined turnover is of at least EUR 40 million, irrespective of the number of employees.[14]

These specialised courts will also have jurisdiction over insolvency proceedings opened in France by foreign companies, pursuant to EU Insolvency Regulation 2015/848.

Thirdly, it is important to note that the court plays a prominent role in insolvency proceedings in France, both in court-governed procedures (such as safeguard) and in out-of-court procedures (such as conciliation). Court involvement is systematic and rather heavy as several judicial authorities are involved, especially in safeguard proceedings. It is optional to appoint a

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[13] A *profession libérale* refers to a person who operates their own economic enterprise.
[14] Commercial Code, Art L721-8.

preliminary judge (*juge commis*) to undertake an audit of the debtor's situation. The judge will gather "all information on the financial, economic and social situation of the company".[15] Where required, the judge may be assisted by any expert of their choosing. The judge's report will serve as the basis for the first ruling made by the court. One or more supervisory judge(s) (*juge-commissaire*) are systematically appointed during the opening order of safeguard proceedings and play a leading role. They have their own jurisdiction and extensive powers, such as the appointment of other actors during the proceedings,[16] as well as the approval and rejection of creditors' claims;[17] rendering them almost omnipresent within insolvency proceedings.[18]

Alongside the court, creditors' representatives (*mandataire(s) judiciaire(s)*) are appointed to represent the creditors' interests and to assess the proofs of claims and valuation of the debtor's debts and assets.[19] They can be assisted by supervising creditors ((*créanciers contrôleurs*) appointed by the insolvency judge.[20]

Self-Assessment Exercise 1

Study the aspects dealt with in the previous section.

France has long been considered to be a debtor-oriented jurisdiction in relation to its insolvency regime. Outline the reasons why this view has come to prevail and explain how this is, or is not, relevant nowadays.

For commentary and feedback on self-assessment exercise 1, please see APPENDIX A

5. SECURITY

Traditionally, two categories of security exist: real and personal security. Personal security includes a letter of intent (*letter d'intention*), a guarantee (*garantie*) and a security bond (*cautionnement*).[21] Their purpose is to add one or more debtors to the principal debtor. Real security, the aim of which is to link one or more assets to a debt, include: (i) movable security: movable liens, pledge, trust, and (ii) immovable security: real estate privilege, pledge, mortgage, and lender's privilege.

What all of these types of security have in common is to confer a privileged situation on a creditor, who is then better off than unsecured creditors.

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15 *Idem*, Art L621-1-4°.
16 *Idem*, Art L621-10.
17 *Idem*, Art L624-2.
18 M Houssin, "Le Droit Français est-il creditor friendly?", *International Journal of Insolvency Law* (2017) (1) 69 76.
19 Commercial Code, Art L621-4.
20 *Idem*, Art L621-10.
21 Civil Code, Art 2287-1.

5.1 Trust (*fiducie*)

A *fiducie* is a situation where one or more persons transfer property, rights or security or a set of property, rights or security, present or future, to one or more trustees who, holding them separate from their own assets, act for a specific purpose for the benefit of one or more beneficiaries.[22]

The main requirement of a *fiducie* is to transfer the ownership of the property initially belonging to the settlor to the trustee, which is a financial institution, an insurance company or a lawyer. These assets are placed in an appropriation account – the fiduciary account – separate from the fiduciary's personal estate. The property that was placed in trust is transferred to the beneficiary at the end of the contract that established the trust. Trust ownership is temporary and is limited to 99 years.

The trust agreement must be registered with the French tax authorities within one month of its execution.

Generally, all types of security are void if the required formalities mentioned above are not complied with (in particular where the security must be created in writing, whether before a notary or not). Non-compliance with the registration requirement renders the security unenforceable against third parties.

The outcome of trust security is that realisation only takes place at the end of the observation period[23] or at the end of the rehabilitation plan. This is because the assets held in trust are considered useful to the company and necessary for its recovery. As a result, the legislator suspends the effects of the trust so that the property remains at the disposal of the settlor.

5.2 Movable lien (*privilège mobilier*)

This type of security confers a right of preference on the creditor in respect of the sale price of the movable asset which forms the basis of the creditor's security, without involving dispossession of the asset.[24]

Article 2331 of the Civil Code lists the general liens. These include, *inter alia*:

- legal costs;
- funeral expenses;
- the remuneration of employees for the last six months; and
- end-of-contract indemnities.

[22] *Idem*, Art 2011.
[23] Discussed below.
[24] Civil Code, Art 2330.

Article 2332 of the Civil Code lists the special liens. These include, *inter alia*:

- all sums due in execution of a lease or the occupation of a building;
- the costs of keeping a piece of furniture; and
- the selling price of a piece of furniture.

Unless otherwise specified, special liens take precedence over general liens.[25] The order of ranking of special liens are determined by Article 2332-3 of the Civil Code.

5.3 Pledge *(gage)*[26]

This is a security interest over a tangible or intangible asset created by contract and can be used to secure the payment of any type of debt. If the debtor defaults, the creditor can either:

- apply for a court order transferring ownership of the pledged asset to the creditor; or
- be paid in cash from the proceeds of auctioning the asset.

At the time that the security interest is created or thereafter, the parties to a pledge agreement can decide that when the creditor wishes to enforce the pledge, it can choose an alternative out-of-court enforcement process (*pacte commissoire*), under which the secured creditor is automatically vested with the title to the property after an expert's appraisal (the expert is appointed by the parties or the court).

Some pledges confer the secured creditor with a right of retention (*droit de retention*) over the pledged asset. The pledged asset is transferred to and retained by the creditor until the debt has been paid in full.

An increasingly common type of pledge with a retention right is one taken over a securities account opened with a bank to record the securities' book entry (*nantissement de compte-titres*). The creditor can retain the securities until it has been paid in full, even if the debtor becomes insolvent and if the court-appointed administrator tries to repossess the securities in order to include it in a sale plan (*plan de cession*).

Generally, there are no specific formalities to create a pledge. However, to ensure that third parties cannot challenge its existence or date of creation, certain types of pledges must be registered with a specific public registry.

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[25] *Idem*, Art 2332-1.
[26] *Idem*, Art 2333.

5.4 Real estate privilege (*privilège de vendeur d'immeuble*)[27]

A real estate privilege is created by operation of law. This privilege is granted for the seller's benefit to secure the portion of the price that cannot be paid in cash. This confers the same rights as a mortgage.

5.6 Mortgage (*hypothèque)*[28]

If the debtor defaults, a mortgage gives the creditor a right to:

- require the sale of the property at a public auction and be repaid out of the proceeds; or
- obtain a court order transferring title to the secured property as payment of its claims; or
- benefit from a priority right (*droit de suite*) if the secured property is sold to a third party without the creditor being notified. If the third party cannot settle the claim, it can be forced to surrender the property to the secured creditor.

The mortgage agreement can also provide that the creditor, in case of default, will automatically be vested with the title to the property after an expert's appraisal (the expert is appointed by the parties or the court).

A mortgage must be created by a deed that is drafted, stamped and executed before a notary or under an agreement deposited with a notary. These formalities are required to ensure validity of the mortgage. As a debtor can grant more than one mortgage as well as privileges over the same immovable property, the deed must be registered with the Mortgage Registry (*Conservation des Hypothèques*) so that the ranking of creditors can be established.

In relation to the enforcement of a mortgage, secured creditors have three possibilities at their disposal:

- The beneficiary of a mortgage may apply to the court for an order to seize the property (*commandement aux fins de saisie*) to be served on the debtor by a bailiff (*huissier de justice*). Following the proceedings to be carried out in accordance with the Civil Enforcement Proceedings Code (*Code des procédures civiles d'exécution*),[29] the property is sold by way of a public auction at a hearing before the court (*tribunal judiciaire*), where bidders must be represented by a legal representative who cannot bid, and neither can the creditor;

- The beneficiary of a mortgage may also apply to the court for the attribution of a court order of the property to the beneficiary of the mortgage, in accordance with a court-monitored allocation process (*attribution judiciaire*) pursuant to Article 2458 of the Civil

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27 *Idem*, Art 2374.
28 *Idem*, Art 2416.
29 Civil Enforcement Proceedings Code, Arts L311-1 *et seq* and R311-1 *et seq*.

Code. This option is not available to the creditor if the property is the main residence of the debtor; or

- Pursuant to Article 2459 of the Civil Code, it may be agreed in the mortgage deed that the creditor is to become the owner of the mortgaged property (*pacte commissoire*). In this case, the value of the property is determined on the day of the transfer by an expert designated by the parties or judicially if no agreement can be reached. This clause is, however, ineffective if the property is the main residence of the debtor.

5.7 Lender's privilege (*privilège de prêteur de deniers*)[30]

A lender's privilege is created by a deed for the benefit of a lender funding the purchase of an immovable property. This privilege confers the same rights as a mortgage. It must be created by a deed and drafted, stamped and executed before a notary. A lender's privilege is usually documented in the same deed as the deed of sale of immovable property, which must be registered with the Mortgage Registry. These formalities are required to ensure validity of the privilege, as well as enforceability against third parties.

5.8 Dailly assignment of receivables (*cession de bordereaux Dailly* or *cession de créances professionnelles à titre de garantie*)[31]

A debtor can transfer present or future debts owed to it by third parties to the creditor, together with all security interests attached to these debts. A Dailly assignment of receivables can only be used if all the following conditions are met:

- the creditor is a credit / banking institution licensed to carry out banking activities in France;
- the receivables are assigned to secure facilities granted in connection with business activities; and
- the assigned receivables arose during business or professional activities.

Claims must be assigned using a special transfer form (*bordereau*) signed by the assignor, describing the amount and type of receivables to be assigned. The assignment comes into effect from the date specified on the form. Failing any agreement to the contrary, the remittance of the transfer form results in the legal assignment of the security interest attached to the assigned receivables to the assignee.

[30] Civil Code, Art 2374.
[31] Monetary and Financial Code, Art L313-23.

The Paris Commercial Court held, in a widely commented upon decision rendered in the *Coeur Défense* case,[32] that a Dailly assignment was enforceable despite the debtor's filing for insolvency.[33]

5.9 Assignment of claims against third parties (*delegation*)[34]

A debtor can transfer claims against its own debtor to the creditor under an agreement between the three parties. This type of assignment can be used when the conditions for the simpler Dailly assignment of receivables are not met. Such an assignment can either be:

- perfect (*parfait*), where the transferred debtor is no longer bound to pay its initial creditor; or

- imperfect (*imparfaite)*, where the transferred debtor continues to be bound to pay its initial creditor and / or the creditor benefiting from the assignment.

5.10 Cash collateral charge (*gage-espèces*)[35]

For this type of security, title to cash collateral is transferred to the creditor. If the debtor defaults, the creditor can set-off all sums owed by the debtor against its (the creditor's) obligation to return the charged cash to the debtor.

5.11 Issues around securities and secured creditors

The practical issues raised by the enforcement of security interests by secured creditors depend on the type of security right, the nature of the asset secured, and the context in which enforcement is requested. This is particularly relevant in case of insolvency proceedings as the rights of secured creditors are generally halted by the stay on enforcement actions and on payments.

Some security interests remain effective. These include security interests which provide exclusivity rights over the assets (for example *fiducie* arrangement without an agreement allowing the settlor to use the assets (*contrat de mise à disposition*), retention rights which ensure that creditors have an exclusive right over the value of the assets (for example pledges over tangible property, pledges over securities accounts, etcetera)).

However, since 1 October 2021, increases in the scope of a consensual security interest or retention right are prohibited when insolvency proceedings are opened. This prohibition covers only the observation period of insolvency proceedings (for an explanation of the concept of "observation period", see below).

[32] Commercial Court of Paris, 19 October 2009 (T. com. Paris, 19 octobre 2009, aff. n° 2009031754, SAS Heart of La Défense c/ Société Eurotitrisation, SA).

[33] This decision was confirmed by the Court of Appeals of Versailles on 28 February 2013 (CA Versailles, 13e ch., 28 févr. 2013, n° 12/02755).

[34] Civil Code, Art 1336.

[35] *Idem*, Art 2374 *et seq.*

Self-Assessment Exercise 2

Study the aspects dealt with in the previous section.

Under French law, a secured creditor can enforce a mortgage in three different ways. Outline these possibilities.

For commentary and feedback on self-assessment exercise 2, please see APPENDIX A

6. INSOLVENCY SYSTEM

6.1 General

French insolvency rules are contained in a single piece of legislation (thus, a unified approach). Provisions relating to corporate insolvency law in France are governed by Title VI, Articles L610-1 to L696-1 of the Commercial Code (*Code de Commerce*).

Generally speaking, France has long been considered too favourable to a debtor and "unreasonably averse to creditors".[36] Even though regular reforms have reinforced the prerogatives of creditors in insolvency procedures,[37] French insolvency law remains internationally known for the comparatively low level of protection afforded to the interests of creditors in comparison to those of other stakeholders.[38] As a result, France ranks quite low in respect of the "strength of its insolvency framework" in international and comparative studies[39] as a result of the limited role of creditors in restructuring proceedings.[40]

In France, the court takes a leading role in insolvency procedures and makes key decisions from the opening to the closing of the judgment. However, over the years, commentators have advocated for an adjustment of the involvement and role of the judge,[41] especially in preventive restructuring proceedings where it has been argued that the debtor and creditors should be left to negotiate a fair settlement on their own.

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[36] F Pérochon, *Entreprises en difficulté* (LGDJ, 2014) at 205.

[37] Law No 2005-845 of 26 July 2005; Ordinance No 2008-1345 of 18 December 2008; Ordinance No 2014-326 of 12 March 2014; Law No 2015-990 of 6 August 2015; and Law No 2016-1547 of 18 November 2016.

[38] G Plantin *et al*, French Council of Economic Analysis, "Les notes du conseil d'analyse economique" No 7 (June 2013) at 1. Available at https://www.cae-eco.fr/en/Les-enjeux-economiques-du-droit-des-faillites.

[39] See, eg, World Bank, *Doing Business Report*, which states that the recovery rate of creditors in a fictious case under consideration was estimated at 74.8% in France, compared to well above 85% in other European countries such as Denmark, Finland, Ireland, the Netherlands, Norway, Slovenia and the United Kingdom.

[40] A Epaulard and C Zapha, "Distressed firms: how effective are preventive procedures?", *France Strategie – La Note d'Analyse* No 84 (February 2020) at 2. Available at https://www.strategie.gouv.fr/sites/strategie.gouv.fr/files/atoms/files/fs-na-84-procedures-preventives-anglais.pdf.

[41] V Rotaru, "The Restructuring Directive: A Functioning Law and Economics Analysis from a French Law Perspective" (30 September 2019) at para 107. Available at https://droitetcroissance.fr/wp-content/uploads/2015/01/Vasile-Rotaru-The-Restructuring-Directive-a-functional-law-and-economics-analysis-from-a-French-law-perspective.pdf.

In France, the insolvency test is a pure cash flow test (referred to as a payment failure situation (*cessation des paiements*)). It is defined as the debtor's inability to pay its debts as they fall due with reference to its immediately available assets, taking into account available credit lines and moratoria.[42] This payment failure situation gives rise to an obligation for the debtor to draft a declaration of payment failure (*déclaration de cessation des paiements*) which must be filed with the registry of the competent court.

In the event that the company's directors were aware of the debtor's insolvency but failed to file the appropriate proceedings within 45 days, they may be held personally liable in tort for an act of mismanagement (*faute de gestion*)[43] and may also be subject to professional sanctions (for example, the prohibition to manage any business for up to 15 years).

Under French law, there are two categories of insolvency proceedings: (i) amicable, out-of-court proceedings, and (ii) court-administered proceedings.

The first category includes *ad hoc* mandate and conciliation proceedings, while the second category includes safeguard, accelerated safeguard, rehabilitation and liquidation proceedings.[44]

6.1.1 Ad hoc mandate

The debtor cannot be insolvent to avail of an *ad hoc* mandate. An *ad hoc* representative (*mandataire ad hoc*) is appointed to oversee the procedure. This representative will make any proposal relevant to the preservation of the business, the pursuit of its economic activity and the preservation of employment.

6.1.2 Conciliation

For conciliation proceedings, the debtor must not have been insolvent for more than 45 days. Conciliation is mostly an out-of-court procedure, opened at the request of the debtor. A conciliator (*conciliateur*) is appointed, who oversees the procedure and makes any proposal relevant for the preservation of the business, its activity and employment.[45] At the end of the process, the conciliation agreement is sanctioned by the court (*constatation* or *homologation*).[46]

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[42] Commercial Code, Art L631-1.

[43] Cass. Com., 5 février 2020, n°18-15.072.

[44] Note that accelerated financial safeguard proceedings no longer exist separately under French law, as Ordinance of 2021 merged them into accelerated safeguard proceedings (whose scope may be limited to financial creditors).

[45] Commercial Code, Art L611-7.

[46] *Idem*, Art L611-9. Before the court sanctions an agreement it must hear the debtor, the creditors who are parties to the agreement, the conciliator and some representatives of the company.

6.1.3 Safeguard proceedings

Safeguard proceedings are a court-based, collective and debtor-in-possession procedure. In order to avail of safeguard proceedings the debtor cannot be in a payment failure situation. The judgment opening the procedure triggers the appointment of:

- an insolvency judge (*juge commissaire*) who oversees the procedure. In complex cases, the court can appoint several supervisory judges;

- an administrator (*administrateur judiciaire*), who supervises and / or assists the management in preparing the plan; and

- creditors' representatives (*mandataires judiciaires*), who represent the creditors' interests and addresses the proofs of claims. They can be assisted by supervising creditors (*créanciers contrôleurs*) appointed by the insolvency judge.

The court sanctions the safeguard plan at the end of the negotiation process after having heard the role-players mentioned above, as well as employees' representatives and the Public Prosecutor.[47]

6.1.4 Accelerated safeguard

This is a variant of the safeguard procedure. It is not a standalone procedure and can only be opened following conciliation proceedings. This procedure bridges out-of-court, amicable proceedings (conciliation) and insolvency proceedings (safeguard) with the idea that restructuring solutions can be negotiated during the amicable phase and implemented in the context of subsequent insolvency proceedings.

6.1.5 Rehabilitation proceedings

This is a court-based, collective, debtor-in-possession procedure. The debtor must be insolvent to avail of the procedure. It can be opened by the debtor, any unpaid creditor or the Public Prosecutor. The judgment opening judicial rehabilitation proceedings triggers the appointment of the same role-players as in safeguard proceedings.

6.1.6 Liquidation proceedings

In liquidation proceedings, the debtor must be insolvent. The objective of the procedure is to appoint a liquidator who will seize and realise the assets of the debtor and distribute the proceeds to creditors. Alternatively, the liquidator can proceed to a sale of the business. The judgment opening the procedure triggers the appointment of:

- an insolvency judge (*juge commissaire*) who oversees the procedure. In complex cases, the court can appoint several supervisory judges;

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[47] *Idem*, Art L626-30-2.

- a liquidator (*liquidateur judiciaire*); and

- creditors' representatives (*mandataires judiciaires*), who represent the creditors' interests and addresses the proofs of claims. They can be assisted by supervising creditors (*créanciers contrôleurs*) appointed by the insolvency judge.

6.2 Personal / consumer bankruptcy

6.2.1 Overview of the procedure

Insolvency proceedings are not applicable to natural persons. Natural persons are subject to a different regime called over-indebtedness of individuals (*procedure de surendettement des particuliers*), governed by the Consumer Code (*Code de la consummation*).[48] This procedure is the counterpart of insolvency procedures that apply only to companies in financial difficulty and it aims to provide solutions for natural individuals unable to meet their financial obligations.

Article L711-1 of the Consumer Code defines over-indebtedness as the evident impossibility for individuals to meet their personal, (meaning, non-professional) debts that are due and payable. The mere fact of owning one's main place of residence, the estimated value of which is equal to, or greater than, the amount of all personal debts due and payable, does not circumvent over-indebtedness. Article L711-1 also states that the over-indebtedness procedure can only be opened by individuals, not by their creditors or the Public Prosecutor. It also provides that the procedure is only available to individuals who have acted in good faith.

In practice, over-indebted debtors are natural persons (employees, pensioners and unemployed persons) who have accumulated a number of financial obligations that exceed their financial ability to repay these obligations (especially through consumer credits (*crédit à la consommation*)) or because of a change in their situation (for example, redundancy, retirement or divorce)).

6.2.2 Types of debts that qualify for bankruptcy

This procedure is only available in relation to personal debts, as opposed to professional debts. Professional debts have been defined as "debts incurred for the needs or in respect of a professional activity".[49] While a recent case has clarified that income taxes do not qualify as professional debts (regardless of the source of income),[50] some uncertainty in the French system regulating over-indebtedness remains. Persons who are not eligible for insolvency procedures, who additionally do not have non-professional debts but who do have debts qualifying as professional, cannot avail of either insolvency procedures or the bankruptcy procedure. Outstanding contributions to the French social security scheme for independent traders and freelancers (*régime social des indépendants*) or to the social security agency (*Unions de*

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[48] Consumer Code, Arts L711-1 to L771-12 and R711-1 to R771-6.

[49] Cass civ 2ème 8 April 2004, n°03-04013; Cass civ 2ème 2 July 2020, n°19-15959.

[50] Cass civ 2ème 4 November 2021, n°20-15008.

recouvrement des cotisations de sécurité sociale et d'allocations familiales) are considered to be professional debts as they concern the social protection of a company's director.

Importantly, however, due to the concept of the unity of the debtor's estate under French law, whilst the existence of professional debts does not allow the debtor to open a bankruptcy procedure, once the over-indebtedness procedure is opened in relation to non-professional debts, professional debts are said to be "re-introduced" into the procedure.[51] Professional debts are however not discharged at the end of the procedure.

6.2.3 The procedure

Individuals must bring their petition before the commissions of over-indebtedness of individuals (*commissions de surendettement des particuliers*). Each commission is composed of:

- the prefect as president;
- the department director of public finance as vice-president; and
- the local representation of the Bank of France (*Banque de France*) as secretary.

The debtor applies to the commission closest to his place of residence. French debtors residing abroad who have creditors established in France may petition the commission closest to the place of establishment of one of their creditors.

As soon as the petition for bankruptcy is filed and until the decision is made, the examining judge (*judge d'instance*) can order a stay on enforcement actions against the debtor's assets.[52] The stay freezes all repayment deadlines.[53] The postponement of the seizure of real estate items in progress can also be ordered.[54] If the petition for over-indebtedness is admissible, the opening of the procedure has the effect of imposing a stay on enforcement actions and prohibiting any new action taken against the debtor[55] until a final bankruptcy decision is made.[56] The stay cannot exceed two years and will depend on the outcome of the procedure. In the event of a bankruptcy plan, the creditors can petition the judge to lift the stay.

6.2.4 The bankruptcy plan

The bankruptcy commission will seek to reach an agreement between the debtor and its creditors through the drafting of an over-indebtedness reorganisation plan, based on three main features:

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51 Cass civ 2ème 15 November 2007, n°05-15094; Cass civ 2ème 23 October 2003, n°02-04113.
52 Consumer Code, Art L721-4.
53 *Idem*, Art L721-5.
54 *Idem*, Art L721-7.
55 *Idem*, Art L722-2.
56 *Idem*, Art L722-3.

(a) the delineation of a *reste-à-vivre*, which is a minimum level of income guaranteed to a person repaying debts. The commission will determine the amount that should be preserved for debtors based on their family expenses, resources (wages, pension and allowances) and financial expenses (rent, children's education, food, utility bills, health expenses, etcetera);

(b) patrimonial measures (for example, the sale of certain properties with a view to preserve the family home, the reduction of expenses, or the reduction in the interests to be paid on certain debts); and

(c) the repayment of creditors' debts in instalments.

The plan must be approved by creditors and cannot exceed seven years, except in the case of the repayment of a loan for the acquisition of the family home, as in this case the sale of the home would be avoided.

In the absence of a plan, the debtor has two options. He can:

(a) make no request, in which case the bankruptcy process ends and the creditors can resume their proceedings against the debtor;[57] or

(b) apply for measures imposed by the bankruptcy commission. These can take the form of:

- imposed measures (rescheduling of debt payments over a maximum period of seven years; reduction of interest rates; and suspension of non-maintenance debts);[58] and

- recommended measures, which are then validated by the court (reduction of the residual real estate debt after the sale of the main dwelling and partial discharge of claims).

These measures cannot exceed seven years and can be challenged by the debtor or the creditors within 15 days.

6.2.5 *Conversion into personal recovery proceedings*

In the absence of a bankruptcy plan, the commission can also decide to open a personal recovery procedure (*rétablissement personnel*) that can be accompanied by liquidation. This procedure is regulated by the Consumer Code.[59]

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[57] *Idem*, Art R733-1.
[58] *Idem*, Arts L733-1 *et seq*.
[59] *Idem*, Arts R741-1 *et seq*.

Personal recovery proceedings without liquidation

If the debtor has no asset or assets which are exclusively composed of goods necessary for his day-to-day life (such as furniture, clothing, kitchen accessories, etcetera) which cannot be liquidated for the benefit of creditors, personal recovery proceedings will be opened without liquidation proceedings.

The decision to open personal recovery proceedings is made by the bankruptcy commission and the debtor's agreement is not required. However, the debtor or creditors may challenge the commission's decision to open personal recovery proceedings without liquidation before the court within 15 days of their notification of the commission's decision.

This procedure results in the discharge of most of the debtor's obligations that arose prior to the opening of the procedure, which the debtor cannot repay due to the lack of sufficient assets. Future debts are not discharged.

Personal recovery proceedings with liquidation

In the event that the debtor has some assets that can be realised for the benefit of creditors, the bankruptcy commission will refer the matter to the court for the purpose of opening a personal recovery procedure with judicial liquidation.[60] Therefore, the main difference between personal recovery with or without liquidation is that the former requires the involvement of the court whereas the latter is decided by the bankruptcy commission.

Personal recovery proceedings with liquidation are opened with the agreement of the debtor[61] and the commission appoints a liquidator. While the procedure resembles that for corporations, personal recovery proceedings with liquidation are simpler than their corporate counterpart.

The bankruptcy commission ensures that the situation of the debtor meets the threshold for the procedure and sends its opinion to the judge who opens the procedure after having verified the good faith of the debtor, and the fact that it is impossible for the debtor to meet his obligations.

The procedure takes place in two stages, being the:

- opening judgment with the possible appointment of a legal representative (*mandataire*); and
- orientation judgment (*jugement d'orientation*).

The opening judgment triggers the divestiture of the debtor, who can no longer assign his property free of charge or against payment without the agreement of the judge or the legal

60 *Idem*, Art R742-3.
61 *Idem*, Art L742-1.

representative if one has been appointed.[62] The debtor is also prevented from increasing his indebtedness, for example by taking out new loans.

Under the orientation judgment, the legal representative firstly draws up an assessment of the economic and social situation of the debtor (for a period of up to six months after the publication of the opening judgment), which includes a statement of declared receivables, a proposed plan where appropriate, detail and valuation of assets and important aspects of the debtor's lifestyle.[63] This has two main consequences for the creditors: their enforcement actions are automatically suspended[64] and their claims must be verified.[65]

The judge eventually pronounces on:

(a) the liquidation of the personal assets of the debtor;[66] or

(b) the closure of the procedure due to insufficient assets (this has the same consequences as a personal recovery without liquidation); or

(c) the implementation of a recovery plan.

In the event that the judge decides on the liquidation of the debtor's assets, he appoints a liquidator responsible for realising the personal assets of the debtor within 12 months of the judgment being made.[67] The debtor is stripped of his rights to his assets and these rights are exercised by the liquidator throughout the liquidation process.[68] Article L112-2 of the Code of Civil Enforcement Procedures (*Code des procédures civiles d'exécution*) lists the assets that cannot be seized, such as movable property necessary for the life and work of the person seized and his family and objects essential to disabled persons or intended for the care of sick persons.

Article R742-20 of the Consumer Code states that the liquidator shall deposit at the Deposits and Consignments Fund (*Caisse des dépôts et consignations*) the sums resulting from the sales which are made. The proceeds of the sale will be distributed among the creditors according to a draft distribution drafted by the liquidator.[69] The liquidator sends the distribution plan to the creditors and the debtor for their approval, and then to the court. The liquidator then proceeds with the distribution. When the liquidation operations are completed, the judge renders a closing judgment for the:[70]

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[62] *Idem*, Art L742-9.
[63] *Idem*, Arti L742-12 and R742-14.
[64] *Idem*, Art L742-7.
[65] *Idem*, Art R742-17.
[66] *Idem*, Arts R742-18 *et seq.*
[67] *Idem*, Art R742-18.
[68] *Idem*, Art L742-15.
[69] Distribution is provided for in Arts R742-42 *et seq* of the Consumer Code.
[70] *Idem*, Art L742-21.

- extinction of the liabilities if the sale of the assets has made it possible to repay all debts; or
- discharge of the debtor's non-professional debts when liabilities remain.[71]

Self-Assessment Exercise 3

Study the aspects dealt with in section 6.2 on personal bankruptcy.

Look at the personal recovery procedure (*rétablissement personnel*). Two types of personal recovery procedures exist. What are they and what are their purposes and differences?

For commentary and feedback on self-assessment exercise 3, please see APPENDIX A

6.3 Corporate liquidation

6.3.1 Overview of the procedure

Liquidation proceedings are applicable to all private entities (including merchants, craftsmen and independent professionals (*professions libérales*)), as well as corporations[72] that are insolvent (in other words, in a state of cessation of payments) and will not continue trading.

The procedure generally consists of the appointment of a liquidator who will realise the assets of the company, or sell the business as a whole or piecemeal, and distribute the proceeds to the creditors.

6.3.2 The opening of the liquidation procedure

For liquidation proceedings to be opened, the debtor:

- must be insolvent, that is, in a payment failure situation (*cessation des paiements*); and
- rescue must be impossible.[73]

Liquidation proceedings can be opened at the request of the debtor, a creditor or creditors and the Public Prosecutor.[74] Debtors must file for liquidation within 45 days after they are officially in a payment failure situation if they have not opened conciliation proceedings.[75]

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[71] However, Art L743-1 of the Consumer Code refers to Art L741-2 which states that "the following are excluded from any discount, rescheduling or cancellation: maintenance debts; the pecuniary reparations allocated to the victims in the context of a criminal conviction; debts resulting from fraudulent operations committed to the detriment of social protection organisations; fines imposed in the context of a criminal conviction".

[72] Commercial Code, Art L640-2.

[73] *Idem*, Art L640-1.

[74] *Idem*, Art L640-5.

[75] *Idem*, Art L640-4.

Several supporting documents must be submitted to the court, which include, *inter alia*:

- annual accounts;
- corporate identification number;
- cash flow statement for the past month;
- number of employees and turnover amount for the past fiscal year;
- statement of claims and debts;
- list of assets and liabilities, as well as any security and collateral; and
- persons who are jointly and severally liable for the company's debts.[76]

Liquidation proceedings can also result from:

(a) the failure of safeguard or judicial rehabilitation proceedings. If, during the observation period of safeguard and judicial rehabilitation proceedings[77] (which lasts for six months once the proceedings have been opened), the administrator realises that the debtor's situation cannot improve and the company cannot be rescued, the proceedings are converted into liquidation proceedings;[78]

(b) the rejection of a restructuring plan or business transfer;[79] and

(c) the impossibility of carrying out a safeguard or rehabilitation plan.

6.3.3 The procedure

Article L640-1 of the Commercial Code states that liquidation proceedings can be opened against a company in a state of cessation of payments, whose recovery is evidently impossible.

The judgment opening liquidation proceedings triggers the appointment of:

- an insolvency judge (*juge commissaire*) who oversees the procedure. In complex cases, the court can appoint several supervisory judges;
- a liquidator (*liquidateur judiciaire*) who is responsible for collecting all of the company's assets and paying the creditors, as well as assessing proofs of claim. They displace the company's management;

[76] *Idem*, Arts R640-1, R.631-1 and R631-2.
[77] *Idem*, Arts L621-3 and L631-1.
[78] *Idem*, Arts L622-10 and L631-7.
[79] See, eg, Cass com 14 May 1996, n°94-21847; Cass com 25 March 1997, n°94-10289; Cass com 6 July 1999, n°97-15017; and Cass com 30 October 2000, n°97-18820.

- creditors' representatives (*mandataires judiciaires*) who represent the creditors' interests and address the proofs of claims. They can be assisted by supervising creditors (*créanciers contrôleurs*) appointed by the insolvency judge; and

- a court bailiff (*huissier de justice*) or a licensed auctioneer (*commissaire-priseur judiciaire*) to carry out an inventory of the debtor's estate at the time of the opening judgment.

Liquidation proceedings trigger an automatic stay of proceedings against the company. All pre-filing creditors are barred from enforcing their rights to obtain payment from the debtor subject to some exceptions:

- Claims secured by a security interest conferring a retention right: the judge may authorise the payment of a pre-filing creditor to obtain from that secured creditor the surrender of the retained pledged asset to the estate;

- Claims assigned by way of a Dailly assignment of receivables: the creditor to which the debtor's receivables have been assigned by way of a Dailly assignment can directly seek payment of those assigned receivables despite any filing for liquidation;

- Claims secured by a *fiducie* agreement: the creditor can enforce its rights over the assets transferred to the trust; and

- Set-off and close-out netting of financial obligations arising under certain financial contracts.[80]

Additionally, if a sale plan for all or part of the business is contemplated, trading parties cannot terminate or rescind their contracts with the debtor.

According to Article L.649-9-I of the Commercial Code the debtor does not remain in possession of the business and its affairs during liquidation proceedings. French commentators have argued that this measure protects the interests of the creditors by contributing to the preservation of their rights and security.[81]

The scope of the dispossession is wide. The liquidator assumes the responsibilities of running the business and has sole authority over the estate of the debtor. The debtor can nonetheless perform certain acts and exercise certain rights which are not included in the liquidator's mandate. For example, the debtor may bring a civil action against a person responsible for a crime or offence perpetuated against the company. The dispossession affects all present and future assets acquired during the liquidation, as well as rights and shares that fall within the debtor's estate. Dispossession only affects the assets included in the debtor's estate by the collective seizure that results from the opening of the proceedings. This means that the dispossession of the debtor does not affect jointly-owned assets, even though the debtor's portion of the asset is subject to the procedure. In these situations, the liquidator must proceed

[80] Commercial Code, Art L.641-3.
[81] F Pérochon, *Entreprises en difficulté* (LGDJ, 2014).

with the division of the jointly-owned asset in order to include the debtor's portion within the estate that is subject to the liquidation proceedings.[82]

The four main tasks of the liquidator in liquidation proceedings are as follows. Firstly, the liquidator will carry out a social task *vis-à-vis* the employees of the company. He will dismiss, for economic reasons, the employees within 15 days of the liquidation judgment. As per French labour law, this means dismissing employment contracts of indefinite duration (*contrats de travail à durée indéterminée (CDI)*) and early termination of contracts of fixed duration (*contrats de travail à durée déterminée (CDD)*). The employees are then provided with all the necessary documents for their unemployment benefits (employment certificate, employer certificate, etcetera). The liquidator will calculate their employee rights (wages, paid holidays, notice, severance pay, etcetera) and the sum is entered on the statement of wage claim that is submitted to the insolvency judge. The liquidator also liaises with the National Wage Guarantee Fund (*Association pour la Garantie des Salaires (AGS)*) which is a fund fed by the employer's contribution in relation to sums due for the payment of employees. The liquidator then pays the employees all amounts due to them, and the corresponding social security contributions. Unless certain thresholds are exceeded (for example in the case of high salaries), employees tend to be paid fully and relatively quickly.

The second task of the liquidator is the verification of claims. If the liquidation proceedings follow a safeguard or rehabilitation process, the administrator may not have completed the verification of claims. This task is thus carried out by the liquidator.

The third aspect of liquidation proceedings is the continuation or undertaking of actions carried out in the interest of creditors. The liquidator may proceed to the recovery of the sums due to the company and agree to the continuation of legal proceedings in progress if these actions lead to the increase of the pool of the debtor's assets.

Fourthly, the liquidator proceeds with the realisation of the assets of the company or the sale of the business. In general, sales carried out by the liquidator will be authorised by an order from the insolvency judge. Two types of sales exist, namely (i) sale by mutual agreement (to a specific interested party), or (ii) sale by public auction.

Finally, the liquidator needs to proceed with the distribution to the creditors. The funds gathered during the sale are allocated to the creditors. The sums held by the liquidator are firstly allocated to the reimbursement of AGS sums, which were considered as "lent" by the AGS to pay the employees. Then, the legal costs of the liquidation proceedings are paid. The so-called privileged creditors are paid next. These usually include post-filing creditors, tax receivables, social organisations' claims, lessors and any banks holding collaterals. If these creditors have been paid in full, unsecured creditors are then paid *pari passu*.

Liquidation proceedings can be terminated either if the creditors have been paid back in full, or if existing assets are insufficient to pay back all creditors. Firstly, Article L.643-9 states that the procedure will automatically terminate when the business and any residual assets have been

[82] Cass. 1ere civ., 29 June 2011, n.10-25098.

sold and the proceeds distributed to creditors by order of priority. Secondly, since the reform of March 2014, Article L.643-9 also provides that termination is possible even where assets have yet to be sold when "continuing the procedure is disproportionate compared to the challenges of realising the assets". Additionally, the debtor, a creditor, the liquidator or the Public Prosecutor can also petition the court to terminate the procedure. Finally, a creditor can also apply to the court to request the closing of the liquidation procedure two years after the date of the opening judgment.

6.3.4 *Simplified liquidation proceedings*

The legislator has instituted a so-called simplified liquidation procedure for small businesses.[83] The procedure is a variant of the normal liquidation procedure which means that unless the law specifies the contrary, the rules applicable to normal liquidation proceedings also apply.[84] Simplified liquidation proceedings aim at speeding up the course of the procedure. In particular, the liquidator can sell the assets without the need to request the approval of the insolvency judge.

Traditionally, the simplified liquidation procedure applied either automatically or optionally. Since the Law of 22 May 2019[85] became effective, the optionality of the procedure has been abolished. This means that the procedure is automatically open to a debtor:

- who has no real estate assets;
- whose turnover is lower or equal to EUR 750,000; and
- whose salaried workforce is lower or equal to five employees.[86]

This situation presupposes that the court has information allowing it to verify whether the criteria are met. If it does have this information at the time that liquidation proceedings are opened, the court will merely specify that simplified liquidation rules are to be followed. If it does not have the required information enabling it to verify that the criteria are met, the court opens normal liquidation proceedings. The president of the court can, later and on the basis of the report drawn up by the liquidator, convert the proceedings into simplified liquidation.[87]

The judicial liquidation procedure is simplified in respect of several essential points:

- Advertising: pursuant to Article R644-1 of the Commercial Code, the decision to apply simplified judicial liquidation rules is not subject to appeal and is not published in the French Gazette (*Bulletin Officiel des annonces civiles et commerciales* (BODACC));

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83 Law No 2005-845 of 26 July 2005.
84 Commercial Code, Art L644-1.
85 Law No 2019-486 of 22 May 2019.
86 Commercial Code, Art L641-2; Art D641-10.
87 *Idem*, Art L641-2.

- Inventory: the realisation of the inventory can be entrusted by the court[88] to the liquidator in the opening judgment and in this case, if the value of the property justifies it, the insolvency judge appoints a technician to carry out a valuation;[89]

- Asset disposals: the liquidator may proceed with the sale of the assets by mutual agreement or by public auction within the first four months following the opening judgment, without an order from the insolvency judge.[90] Beyond this point, assets are sold at auction;[91] and

- Verification of claims and the distribution: Only claims likely to be of a so-called "useful rank" and employees claims are verified. Useful rank means claims that are likely to be paid back. The liquidator files a statement of these claims with a draft of the distribution, which is published in the official bulletin.[92] The liquidator then proceeds with the distribution.

Self-Assessment Exercise 4

Study the aspects dealt with in the previous section.

Consider the timeline of liquidation proceedings. The liquidation procedure is not constrained by any legal timeframe, except in the case of simplified liquidation proceedings. The duration of simplified liquidation proceedings cannot exceed twelve months (which can in exceptional circumstance be extended by three months). In your opinion, why is it beneficial for liquidation proceedings to be as speedy as possible?

For commentary and feedback on self-assessment exercise 4, please see APPENDIX A

6.4 Corporate rescue

France has long been known as a restructuring-biased jurisdiction, with currently no less than five rescue procedures within its toolbox, namely:

- *ad hoc* mandate (*mandat ad hoc*);

- conciliation (*conciliation*);

- safeguard (*safeguard*);

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88 *Ibid*.
89 *Idem*, Art L644-1-1.
90 *Idem*, Art L644-2.
91 *Ibid*.
92 *Idem*, Art L644-4 and Art R644-2.

- accelerated safeguard *(sauvegarde accélérée)*; and
- rehabilitation procedure (*redressement judiciaire*).

6.4.1 Out-of-court, amicable proceedings: ad hoc mandate and conciliation

French corporate rescue law is comprised of two voluntary, amicable and confidential procedures: *ad hoc* mandate and conciliation, both governed by Articles L611-1 to L611-16 of the Commercial Code. Both procedures were introduced in 2005 and their objectives are to encourage companies that are not yet insolvent to negotiate workouts with their creditors at an early stage and on a confidential and contractual basis. They both allow the debtor to remain in control of its affairs[93] while nominating an insolvency practitioner who will oversee the negotiations. An *ad hoc* representative (*mandataire ad hoc*) or conciliator (*conciliateur*) is chosen by the debtor or appointed by the relevant court.[94] The conciliator will make any proposal that is relevant to the preservation of the business, the pursuit of its economic activity and the preservation of employment.[95]

The main difference between both proceedings is that a conciliation agreement is ratified by the court at the request of the debtor. The court can either approve the agreement (*constatation*), which means that the confidentiality of the procedure is preserved, or it can sanction the agreement (*homologation*), which involves publicising the judgment.[96] In the latter case, the adverse effect of publicity is mitigated by the fact that the sanctioning confers more legal advantages than a mere approval in the event of subsequent insolvency proceedings being opened. In particular, if the conciliation proceedings are converted into accelerated safeguard proceedings, new money providers will benefit from a new money privilege (*privilège de conciliation*).[97] This is granted to investors injecting new money, goods or services into a business during conciliation proceedings which have been sanctioned through *homologation* by the court. These investors will enjoy a priority of payment over all pre- and post-commencement claims in the event of subsequent court-administered proceedings. Such claims benefitting from this new money privilege may also not be rescheduled or written-off by a safeguard or rehabilitation plan without their holders' consent (not even through a cram-down or cross-class cram-down).

6.4.2 Court-assisted proceeding 1: the safeguard procedure

6.4.2.1 Safeguard

The safeguard procedure was also introduced by the Law of 2005 and subsequently reformed in 2008, 2014 and 2016. Modelled on Chapter 11 of the United States (US) Bankruptcy Code,

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93 *Idem*, Art L611-7.

94 *Ibid*.

95 The court can sanction the agreement through *homologation* only if certain conditions are met, including that the provisions of the agreement aim to ensure the viability of the going concern of the company. See Commercial Code, Art L611-8 in this regard.

96 Before the court sanctions an agreement, it must hear the debtor, the creditors who are parties to the agreement, the conciliator and some representatives of the company. See Commercial Code, Art L611-9 in this regard.

97 Commercial Code, Arts L611-11; L626-20; and L626-30-2.

the procedure was originally introduced as an insolvency procedure where the debtor was required to show that it was facing "difficulties that it was not able to overcome" and which would lead to a payment failure situation. The Ordinance of 2008 relaxed this criterion, rendering safeguard available to a debtor who is encountering difficulties which it is not in a position to overcome, while not yet in a payment failure situation. It thus transformed the safeguard procedure into a hybrid mechanism, which can also serve as a preventive restructuring process.

Compared to the *ad hoc* and conciliation procedures, safeguard exhibits characteristics more similar to formal insolvency proceedings. For example, it is not confidential and must involve all creditors. It triggers a stay on enforcement actions[98] during which a rehabilitation plan is proposed (*plan de sauvegarde*).[99] While the debtor remains in possession, the judgment opening the procedure triggers the appointment of an administrator (*administrateur judiciaire*).

The court can only be petitioned by the debtor company who requests the opening of the procedure. While the debtor remains in possession, the judgment that opens the procedure will designate:

- an administrator (*administrateur judiciaire*) who supervises and / or assists the management to prepare the plan;
- an insolvency judge (*juge commissaire*) who oversees the procedure; and
- a creditors' representative (*mandataire judiciaire*) who represents the creditors' interests and assesses the proofs of claims and valuation of the debtor's debts and assets.[100] The creditors' representative can be assisted by supervising creditors (*créanciers contrôleurs*) appointed by the insolvency judge.

The judgment pronouncing the safeguard triggers the opening of a so-called observation period (*période d'observation*) which lasts for six months (renewable once by judgment of the court and, if necessary, a second time, at the request of the Public Prosecutor). The objectives of the observation period are to:

- make a detailed assessment of the state of the company in respect of all important features (for example, cashflow, accounting, operations, social, commercial and legal aspects of the company, etcetera). The administrator and the creditors' representative will draw up reports to inform the court, the insolvency judge and the Public Prosecutor of the state of the company;
- research and implement, if possible, the necessary restructuring measures that will support the rescue of the company; and

98 *Idem*, Art L622-7.
99 *Idem*, Art L621-3.
100 *Idem*, Art L621-4.

- determine the amount of debts that will need to be repaid during the rescue process once the observation period ends. The creditors' representative proceeds alongside the management and, if necessary, the company's accountant, to verify the claims before reporting to the insolvency judge.

The observation period brings with it a stay on enforcement actions while the company continues to trade. However, while the company is therefore temporarily relieved from repaying its debts and free from legal proceedings, the observation period cannot lead to a worsening of the situation, and the company needs to ensure the payment of post-judgment debts.

Even though there is no legal obligation to do so, it is common for the court to set, in its opening judgment, the date for a future hearing a few weeks after the opening judgment. This first hearing tends to be a control hearing, ensuring that the company is in a position to continue its activity without generating new debts. This hearing is purely administrative if the company normally settles its new debts and benefits from an accounting follow-up. However, if the court is not convinced regarding the cashflow of the company (that is, if the court believes that the situation of the debtor will worsen during the safeguard process), it will put an end to the activity of the company.

In relation to the roles of the administrator and creditors' representative during the observation period, the creditors' representative will take care of the past claims of the company, (that is, the pre-petition claims), while the administrator takes care of the future of the company (that is, the preparation of a safeguard plan while ensuring that new debts are not created). More precisely, the legal representative will be in charge of the verification of claims. Creditors are invited to inform the representative of the amount of their claims. The legal representative may then send a statement of claims to the company's management so that the sums requested are verified. The creditors' representative (and the insolvency judge in case he so insists) will deal with any dispute. The administrator, on the other hand, is appointed to support the company in its restructuring endeavour. Ultimately, the purpose of the observation period is, through forecast documents, to obtain an idea of the amount that the debtor has available in order to repay its creditors.

During the observation period, therefore, the information from the creditors' representative, the statement of liabilities and the information resulting from the forecasts gathered by the administrator, form the basis of the drafting of a safeguard plan. In principle, the plan can include different restructuring mechanisms, such as a proposal for full repayment over several years, or a shorter repayment period but including a partial debt forgiveness (as long as the maximum repayment period for creditors does not exceed 10 years). The terms of the plan are proposed to the creditors by way of written consultation (or a meeting), who vote on the plan.

Until the Order of September 2021 transposing the EU Directive on Preventive Restructuring 2019,[101] Article L626-30-2 of the French Commercial Code provided that creditors be grouped within the three following committees:

[101] Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency

(1) credit institutions;

(2) main suppliers; and

(3) bondholders.

The French position had been heavily criticised by commentators over the years for its lack of homogeneity of interests, with senior, junior, privileged and unsecured creditors being grouped in the same committees[102] and for not meeting international standards when complex financing schemes involving different layers of debt were involved.[103]

In the period leading up to the transposition of the Directive, debates around class formation were numerous. Some authors suggested that classes should be divided into sub-categories based on a commonality of interest, as is the case in Chapter 11 of the US Bankruptcy Code;[104] while other commentators mentioned the possibility for the government to introduce a specific class for new money providers or a one-person class comprised of one creditor only,[105] as well as a class grouping all shareholders who could vote on the safeguard plan but could also be crammed-down with a view to deterring them from unreasonably preventing or creating obstacles to the adoption of a restructuring plan.

In introducing classes of creditors in September 2021, the Commercial Code also introduced a difference between safeguard and accelerated safeguard proceedings. In the latter, the formation of classes is compulsory for all debtors.[106] For safeguard proceedings, however, the new class system is not mandatory except for companies that meet the following thresholds:

(a) they employ over 250 employees and have a turnover greater than EUR 20 million; or

(b) they have a turnover of over EUR 40 million.[107]

These thresholds are higher than those that applied to the former creditors' committees and it is therefore anticipated that their formation will remain relatively marginal in number. The thresholds reflect delicate political choices between equal access to restructuring tools and

of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency), O.J. L 172/18.

[102] V Rotaru, "The Restructuring Directive: A Functional Law and Economics Analysis from a French Law Perspective" (September 30, 2019); para 12: "current French law provides, contrary to any common sense, that any safeguard plan must be voted on by creditors organized in three separate bodies".

[103] R Dammann and M Boché-Robinet, ''Transposition du projet de directive sur l'harmonisation des procédures de restructuration préventive en Europe. Une chance à saisir pour la France'' (2017) Recueil Dalloz No 22 (June 22, 2017).

[104] A Droege Gagnier and A Dorst, ''France: *quo vadis*? France is keen to reform its security and insolvency law.'' (2018) 12 *Insolvency and Restructuring International* 24, 25.

[105] See R Dammann and A Alle, "Directive 'Restructuration et Insolvabilité': l'introduction des clas- ses de créanciers en droit français" (2019) Recueil Dalloz 2047 *et seq*.

[106] Commercial Code, Art L628-4.

[107] *Idem*, Arts L626-29 and R626-52.

greater or lesser complexity of the procedures depending on the size of the debtor.[108] At the request of the debtor, the supervising judge (*juge-commissaire*) may nonetheless constitute classes of affected parties for debtors that fall below the threshold. The decision is a measure of judicial administration and is not subject to appeal.[109]

Second, considerable leeway is left to the insolvency practitioner who will group creditors within classes representative of a sufficient commonality of economic interests (*communauté d'intérêt économique suffisante*). This will therefore vary depending on the typology of the company's liabilities and its activity. At the very least, however:

(a) creditors whose claims are secured by security interests *in rem* and other creditors (such as unsecured ones) must belong to different classes;

(b) the class formation must comply with subordination agreements entered into before the commencement of proceedings;

(c) equity holders must make up one or more classes; and

(d) in relation to creditors secured by a trust (*fiducie*) granted by the debtor, only the amount of their claims not secured by such security, is considered.[110]

Tax and social creditors are not part of any classes, nor are the employees. The administrator notifies each affected party of their grouping and class.[111] In the event of disagreement concerning the affected parties, the methods of distribution into classes and the calculation of the votes, each affected party, the debtor, the public prosecutor, creditors' representatives or the administrator may petition the supervising judge.[112]

The consultation involves the submission of a draft plan prepared by the debtor with the assistance of the administrator for consideration by the affected parties.[113] The creditors' representatives and the employment councils (or employee representatives) present their observations to the classes.[114] It is the debtor or the administrator who sets the date at which the classes will vote on the proposals.[115]

On that date, each class (if they have been constituted) casts a vote under the conditions provided for by law in Article L626-30-2 of the Commercial Code. The plan is approved if two-thirds of the amount of claims held by the voters of the class concerned have voted positively.

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[108] O Buisine and V Rousseau, '"L'efficacité des procédures de restructuration, d'insolvabilité et de seconde chance': commentaire du titre IV de la directive Restructurations préventives'', Rev. proc. coll. 2020, no 2, study 10.
[109] Commercial Code, Arts L626-29 and R626-54.
[110] *Idem*, Art L626-30.
[111] *Idem*, Art R626-55.
[112] *Idem*, Art R626-58-1.
[113] *Idem*, Art L626-30-2.
[114] *Idem*, Art R626-59.
[115] *Idem*, Art L626-30-2.

Once the creditors have voted on the plan, the court will either:

(a) sanction the plan if it considers that the proposals are appropriate and that the company has a chance of survival. The court also designates a commissioner for the execution of the plan, who will either be the administrator or the creditors' representative; or

(b) reject the plan.

If the plan is not approved, it may nonetheless be sanctioned by the court, at the request of the debtor or the administrator (with the agreement of the debtor) and be imposed on dissenting classes.[116] This is known as the possibility to cross-class cram-down dissenting creditors.

With the introduction in 2021 of the possibility to cross-class cram-down dissenting creditors during safeguard proceedings, came the introduction of safeguards ensuring that all parties are treated fairly, especially creditors. First, the debtor's consent is compulsory for the court to cross-class cram-down creditors.[117] Second, France has adopted the absolute priority rule, which means that creditors of a class that voted against the plan must be fully repaid when a lower-ranking class is entitled to be paid or retains an interest. However, the court may make exceptions to this requirement (for example, in the case of strategic suppliers, tort claimants or equity holders) if such exceptions are deemed necessary to achieve the plan's objectives and if the plan does not excessively affect the rights or interests of impaired parties.[118] Third, in order to adopt a restructuring plan despite the negative vote of one or several classes of creditors, and therefore effect a cross-class cram-down, the court must verify that one of the following two criteria are met:

(a) a majority of the classes of impaired parties voted in favour of the plan, provided that at least one of those classes is a secured creditors' class or is senior to the ordinary unsecured creditors' class;[119] or

(b) at least one of the classes of affected parties has voted favourably, that is, a class other than an equity holders' class or any other class which is "in the money" (that is, which, after determining the value of the debtor as a going concern, could reasonably be expected not to be entitled to any payment or retain any interest while applying the normal distribution order as would be the case in liquidation proceedings or a sale plan (*plan de cession*).[120]

Finally, the court must ensure that when affected parties have voted against the draft plan, none of these affected parties is in a less favourable situation because of the plan, than that which they would be in in a liquidation or sale of the company.[121]

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[116] *Idem*, Art L626-32.
[117] *Idem*, Art L626-32.
[118] *Idem*, Art L626-32-I-3° and L626-32-II.
[119] *Idem*, Art L626-32-I-2°-a).
[120] *Idem*, Art L626-32-I-2°-b).
[121] *Idem*, Art L626-31.

When one or more classes of equity holders have been constituted and have not approved the plan, a cross-class cram-down may only be implemented if:

(a) the debtor exceeds a certain threshold (that is,150 employees or more or a turnover of EUR 20 million or over);

(b) the equity holders of one or several dissenting classes are not "in the money";

(c) if the plan provides for a capital increase subscribed by cash contribution or by set-off against receivables, the shares issued are offered in priority to the shareholders, *pro rata* their existing shareholding;

(d) the plan does not provide for the transfer of all or part of the rights of dissenting class(es) of equity holders.[122]

The Order of September 2021 also introduced a "post-money" (post-commencement funding) privilege which did not exist previously. This privilege benefits claims arising from a cash contribution to the debtor:

(a) during the observation period, authorised by the supervisory judge; and / or

(b) for the implementation of the safeguard plan adopted by the court; or

(c) for a modification of the plan, adopted by the court.[123]

Claims guaranteed by the "post-money" privilege (*privilege de post money*) cannot be subject to write-off or postponements which are not agreed by their holders in the event of subsequent restructuring proceedings. These claims can thus only be overridden by certain specific claims, such as the super-priority granted to wages, legal fees, new money privileged claims and post-petition claims of the National Wage Guarantee Fund (*Association pour la Garantie des Salaires* (AGS)).

At any time during the observation period and, in particular, if no solution is possible or if new debts arise, the court may order rehabilitation or liquidation proceedings to be opened.

6.4.2.2 Accelerated safeguard

In the immediate aftermath of the global financial crisis of the late 2000s, developments in legal practice prompted some reforms of the French landscape. Debtors wishing to benefit from an arrangement similar in structure to a pre-pack were negotiating an agreement before entering into safeguard proceedings. The agreement negotiated would then be adopted in the form of

[122] *Idem*, Art L626-32-I- 5°.
[123] *Idem*, Art L622-17.

a safeguard plan. To codify existing practices, the accelerated safeguard was introduced in 2014 as a pre-pack variant of safeguard.

The Order of 15 September 2021, transposing the EU Directive on Preventive Restructuring Frameworks 2019, made the accelerated safeguard procedure the core framework of preventive restructuring within the meaning of the Directive. It meets the European legislator's expectations of ensuring a vote on a restructuring plan in a short timeframe, thanks to the compulsory passage through conciliation first. With a maximum duration of four months, accelerated safeguard proceedings are now available to all companies, regardless of their size, which was not the case before October 2021. The objective of the accelerated safeguard procedure is, therefore, to preserve the company's value within the framework of a so-called pre-pack, where a restructuring plan can be adopted by affected creditors.[124]

Importantly, accelerated safeguard is not a standalone procedure. Rather, accelerated safeguard proceedings are opened at the request of a debtor who can demonstrate that:

(1) they are engaged in the conciliation procedure;

(2) a conciliation agreement has been drawn up, aimed at ensuring the sustainability and rescue of the company; and

(3) the agreement must be likely to receive support from the affected parties within two months of the opening judgment.[125]

The objective here is for the debtor to reach an agreement with its creditors in a speedy fashion.

Subject to some variations, found in Chapter VIII of Book VI of the Commercial Code, the accelerated safeguard is subject to the rules applicable to the traditional safeguard. The first substantial variation is that, to open safeguard proceedings, the debtor must be engaged in conciliation proceedings.[126] The fact that the debtor is in a payment failure situation does not preclude the opening of accelerated safeguard; the same criterion is used as that of the conciliation, that is the debtor must not have been in a payment failure situation for more than 45 days.[127] The decision to open accelerated safeguard proceedings is taken by the court on the basis of the report prepared by the conciliator, expressing their own opinion on the likelihood of the restructuring plan being adopted by the creditors concerned.[128]

The plan is therefore prepared, and receives the approval of affected parties in sufficient numbers to ensure its approval, during conciliation proceedings. The attractiveness of the two-

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[124] The replacement of the concept of committees by *classes* of creditors, led to the disappearance of the accelerated financial safeguard because the committee of credit institutions no longer exists. However, it is still possible to limit the effect of accelerated safeguard proceedings to financial creditors only (Art L628-1 of the Commercial Code).

[125] Commercial Code, Art L628-1.

[126] *Idem*, Art L628-1.

[127] *Ibid*.

[128] *Idem*, Art L628-2.

stage approach of the conciliation and accelerated safeguard preventive restructuring framework is that it combines confidentiality and contractual flexibility during the conciliation phase with the possibility for the court to bind dissenting creditors in the safeguard phase of the procedure through a cross-class cram-down process.[129] It also protects new financing brought forward during the conciliation process (*privilege de conciliation*) if the conciliation agreement has been sanctioned (*homologation*) by the court. Investors will enjoy a priority of payment over pre- and post-commencement claims in the event of subsequent court-administered proceedings. Such claims benefitting from this new money privilege cannot be rescheduled or written-off by a safeguard or rehabilitation plan (*plan de sauvegarde / plan de redressement judiciaire*), without their holders' consent, not even through cram-down or cross-class cram-down.

Overall, the voting conditions and adoption of the plan by the classes of affected parties are defined within the framework of the traditional safeguard, which remains the flagship of Book VI of the Commercial Code. The specificities of the accelerated safeguard, therefore, lie in the compulsory constitution of classes of affected parties (which is not the case under safeguard proceedings) and the imposition of a short deadline, since the plan must be adopted within two months of the opening judgment, otherwise the procedure is closed, without possible conversion.[130]

6.4.3 *Court-assisted proceeding 2: the rehabilitation procedure*

Title III of Book VI of the Commercial Code regulates the rehabilitation procedure, introduced by Law Number 85-88 of 25 January 1985, supplemented by Decree Number 85-1389 of 27 December 1985. Rehabilitation proceedings follow the rules of the safeguard procedure with some departures. Generally, the main difference between the safeguard and the rehabilitation procedures lies in the nature and severity of the difficulties encountered. For rehabilitation proceedings to be opened, the company needs to be in a payment failure situation, which amounts to difficulties which are more severe than the possible momentary cash flow problem under safeguard.

Similar to safeguard, when the debtor is insolvent and rescue does seem likely, the management of the distressed company can request the opening of rehabilitation proceedings no later than 45 days from the date on which it becomes insolvent, provided that conciliation proceedings are not pending.[131] Any unpaid creditor or the Public Prosecutor may also request the court to open rehabilitation proceedings against the debtor.[132]

Similar to the safeguard, the objectives of rehabilitation proceedings are to allow the company to keep trading, preserve employment and pay off the company's liabilities. It gives rise to a plan sanctioned by a court at the end of the observation period and, where appropriate, to the constitution of classes of affected parties.[133]

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[129] *Idem*, Arts L628-8 and L626-31.
[130] *Idem*, Art L628-8.
[131] *Idem*, Art L631-4.
[132] *Idem*, Art L631-5.
[133] *Idem*, Art L631-1.

Rehabilitation proceedings are available to the same debtors who qualify for safeguard proceedings. The insolvency judge opens a six-month observation period, renewable for up to 18 months[134] (compared to a maximum of 12 months under safeguard proceedings), during which the debtor negotiates a restructuring plan with its creditors.

During the observation period of rehabilitation proceedings, all secured and unsecured creditors are subject to a stay on enforcement actions and legal individual proceedings against the company for proceedings or claims that arose before the opening judgment. However, in order to be stayed, legal proceedings or enforcement actions must be related to a default of cash payment. Otherwise, legal proceedings or enforcement actions related to a specific performance (*execution forcée en nature*), such as the release of a document, the termination of a contract or the reimbursement of defective hardware, are not subject to the stay.

During the observation period of rehabilitation proceedings, the court appoints an administrator who is in charge of assisting the management of the debtor who will continue the daily management of the business while the administrator supervises such management. In rehabilitation proceedings, the administrator has the exclusive power to continue or terminate the debtor's contracts. The administrator may request the termination of a contract, if it is deemed necessary to safeguard the debtor and if the contract involved does not excessively prejudice the other party's rights. If contracts are continued, the debtor and the creditor remain in the same situation that existed prior to the opening of the rehabilitation proceedings. The creditor shall continue to honour its commitments, despite the default of payment by the debtor prior to the proceedings. If the contract is rejected, the effect may also be favourable to the debtor since the burden of repayment is reduced.

At the end of the observation period, the judge will make an order for:

- the continuation of the business through a rehabilitation plan;
- the sale of all or part of the debtor's assets through a sale plan; or
- if the latter fails, conversion into liquidation proceedings.

Safeguard rules apply in relation to creditors' voting on the rehabilitation plan. Classes of creditors may be created depending on the size of the company and the voting majority is two-thirds. However, differences to the safeguard process also exist:

- if the debtor does not meet the required thresholds, the authorisation to form classes of affected parties may be requested by the administrator from the insolvency judge, without the debtor's approval;
- any affected party may submit a draft plan to the vote of the classes;

[134] *Idem*, Art L631-7.

- if the plan has not been approved by all classes of affected parties, the court can decide to apply the cross-class cram-down mechanism at the request of any affected party (in addition to the debtor or the administrator with the debtor's consent); and

- if the plan approval through the class-based consultation procedure (whether by regular approval by the classes of affected parties or by a cross-class cram-down) is not achieved, the approval may occur through individual consultation rules.

In 2015, the Macron Law provided the court with new powers in rehabilitation proceedings opened from 7 August 2015 in respect of certain companies. After a period of three months following the opening of rehabilitation proceedings, the court may order either:

(i) a forced increase of capital (*mécanisme de "dilution forcée"*); or

(ii) a forced sale of opposing shareholders' shares ("*cession forcée*") at the administrator's or at the Public Prosecutor's request, under the following conditions:

  - the company has at least 150 employees or is a dominant company (*entreprise dominante*) in the sense of the French Labour Code (*Code du travail*) over one or more companies employing at least 150 employees; and,

  - the cessation of the business of the company is likely to cause a serious harm (*trouble grave*) to the national or regional economy and to employment; and

  - the change in the company's share capital appears to be the only serious option to avoid such harm and to allow the continuation of business after the chances of total or partial sale have been examined; and

  - the affected parties refused to adopt the changes in the company's share capital provided for in the proposed rehabilitation plan in favour of one or several persons committed to perform the plan.[135]

If a forced increase of capital is decided, the court may appoint a person (*mandataire*) whose mission is to convene a shareholders' meeting and to vote on the proposed capital increase up to the amount provided for in the rehabilitation plan, in place of the opposing shareholders; the capital increase must be carried out within a maximum period of 30 days after the vote. It may be released by the persons who committed themselves to perform the plan by set-off with the claims of the company which have been admitted and limited to their reduction within the plan.[136]

If a forced sale of shares (*cession forcée*) is ordered, those shareholders who agreed to perform the proposed plan will be the acquirers of all or part of the shares of the shareholders who refused the capital modification and who hold, directly or indirectly, shares giving them the

[135] *Idem*, Art L631-19-2.
[136] *Idem*, Art L631-19-2-1°.

majority of the voting rights or a blocking minority in the general meetings of the company or have controlling powers by application of an agreement concluded with other shareholders and which is not contrary to the social interest; any provision requiring formal approval (*clause d'agrément*) is deemed null and void. In this situation, any shareholder, other than those described above, is entitled to withdraw from the company and simultaneously request its shares to be redeemed by the transferees.[137]

When the court is seized of a sales request, in case no agreement has been found by the interested parties on the value of the shares at stake, such value will be determined by an expert appointed by the President of the Court at the request of the most diligent party, of the administrator or of the Public Prosecutor.

Therefore, although the safeguard proceedings are available to solvent debtors and rehabilitation proceedings to insolvent ones, the similarities of these two regimes meant that very comparable restructuring tools were applied to companies in very different situations (solvent or insolvent). The Ordinance of 15 September 2021 has slightly modified these proceedings, as the government opted to use the accelerated safeguard as the main vessel for the transposition of the PRD 2019. However, since safeguard proceedings are in practice often used defensively to protect a company facing financial difficulties, or as a threat in upstream negotiations, the French government has chosen to introduce additional distinctions between the safeguard and rehabilitation procedures:

(i) the maximum duration of safeguard proceedings has been lowered to 12 months (it used to be 18 months before the Ordinance of 2021), whereas rehabilitation proceedings can last for up to 18 months;[138]

(ii) while the safeguard rules also apply to creditors' voting and classes, differences have now been introduced of the rehabilitation procedure:

  (a) if the debtor does not meet the required thresholds, the authorisation to form classes of affected parties may be requested by the administrator, without the debtor's approval;[139]

  (b) any affected party may submit a draft restructuring plan to the vote of the classes;[140]

  (c) if the plan has not been approved by all classes of affected parties, the court can decide to apply the cross-class cram-down mechanism at the request of the debtor or any affected party (in safeguard proceedings, the cross-class cram-down can be implemented by the court with the approval of the debtor only);[141] and

[137] *Idem*, Art L631-19-2-2°.
[138] *Idem*, Art L631-7 and Art L621-3 for the safeguard.
[139] *Idem*, Art L631-1.
[140] *Idem*, Art L631-19.
[141] *Ibid*.

(d) if the approval of the plan through the class-based consultation procedure (whether by regular approval by the classes of affected parties or by a cross-class cram-down) is not achieved, the approval may occur through individual consultation of the creditors;[142]

(iii) finally, where the plan is not approved by the requisite classes, including through a cross-class cram-down, the court's power to reschedule the debtor's liabilities by up to ten years (also known as "term-out") is no longer available in safeguard proceedings[143] but remains available in rehabilitation proceedings. This is however subject to a minimum instalment of 10% after the fifth year, thereby providing debtors with stronger leverage in restructuring discussions.[144]

Self-Assessment Exercise 5

Study the aspects dealt with in the previous section.

Question 1

Consider the preventive reference framework that is the combination of conciliation proceedings with accelerated safeguard proceedings. This framework is considered to be a pre-pack option for distressed debtors. Outline how this framework works and discuss the specific features attached to both the conciliation phase and the accelerated safeguard phase.

Question 2

Whilst the safeguard procedure and rehabilitation process exhibit many similarities, recent reforms have sharpened their differences. What are the main differences between the safeguard and the rehabilitation procedures?

For commentary and feedback on self-assessment exercise 5, please see APPENDIX A

7. CROSS-BORDER INSOLVENCY LAW AND THE RECOGNITION OF FOREIGN JUDGMENTS

International and cross-border insolvency law raises two main questions of jurisdictional competence from the point of view of the French legal system:

(i) when are French courts competent to deal with a situation of cross-border insolvency and, in particular, when are they competent to initiate proceedings against an insolvent company that has assets, creditors or even managers abroad?

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[142] *Ibid*.
[143] *Idem*, former Arts L621-62 *et seq*.
[144] *Idem*, Art L626-18.

(ii) under what conditions can a French court recognise, and give effect to, an insolvency judgment delivered by a foreign court?

The main legislation that applies to cross-border restructuring and insolvency cases involving France and other EU member states, is EU Regulation 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (Recast) (EU Insolvency Regulation).

The EU Insolvency Regulation applies within the EU (other than Denmark) to public insolvency proceedings as defined therein and listed in its Annex A (including safeguard, accelerated safeguard, rehabilitation and liquidation proceedings). It provides that the courts of the member state in which a debtor's centre of main interests (COMI) is situated will have jurisdiction to commence the main insolvency proceedings relating to such debtor. The determination of a debtor's COMI is a question of fact on which the courts of the different member states may have differing and even conflicting views.

The COMI is the place where the debtor conducts the administration of its interests on a regular basis and which is ascertainable by third parties. The presumption that the COMI is the place of the registered office will not apply if the registered office has shifted in the preceding months.

When the other country is one of the EU member states (excluding Denmark), the European texts applicable to this matter, and particularly the EU Insolvency Regulation, are based on the principle of the immediate and automatic recognition of decisions relating to the opening, running and closing of the insolvency proceedings in all other EU member states without any special procedure or declaration of enforceability required.

If a company's COMI is in France, the main proceedings can be commenced before the French court under the EU Insolvency Regulation. A company's COMI is presumed to be the place of its registered office unless it is proven that both:

- its COMI, as defined in the *Eurofood* decision of the European Court of Justice,[145] is in a country other than its place of incorporation; and

- the company's trade and financial partners are aware that the COMI of such company is not its place of incorporation.

Secondary proceedings can subsequently be commenced with respect to an establishment located in another EU member state. Secondary proceedings under the EU Insolvency Regulation are also appropriate if a company has an establishment in France, but its COMI is in another EU member state.

In the *Mansford* case,[146] several Luxembourg holding companies filed for safeguard in France on the ground that their COMI was in France. In early 2010, the Paris Court of Appeal, applying

[145] Case C-341/04, *Eurofood IFSC Ltd*.
[146] Paris Court of Appeal, 25 February 2010.

the rationale of the *Eurofood* decision, held that French courts had jurisdiction over the matter for the following reasons:

- all management and other meetings were held either in Paris or locally where the real estate assets were located;

- the companies had no assets or activities other than a property asset and a letting activity in France (no activity in Luxembourg);

- the two holding companies' sole purpose was to hold 100% of their 10 subsidiaries;

- the ultimate parent company's sole purpose was to own 100% of holding companies that had no activity in Luxembourg; and

- the relationship with the lenders was initiated in France and the renegotiation of the financing documentation took place in France.

Under the EU Insolvency Regulation, foreign creditors benefit from the following specific provisions:

- an additional delay of two months to file their claims (four months compared to two months for French creditors) from the date of publication of the opening judgment in the French Gazette (BODACC); and

- in accordance with the EU Insolvency Regulation, the opening of insolvency proceedings in France will not affect the rights *in rem* of creditors or third parties in relation to tangible or intangible, movable or immovable assets, nor specific assets and collections of indefinite assets as a whole which change from time to time, belonging to the debtor and that are situated within the territory of another member state at the time of the opening of proceedings.

Self-Assessment Exercise 6 (Cross-Border Insolvency)

Prêt A Jouer (PAJ) is a France-registered toy shop company. The company opened its first store in Strasbourg in 2011. One of PAJ's warehouses is in Madrid (Spain) and PAJ rents out this warehouse to other toy companies. In 2013, PAJ concluded a line of credit agreement with a Spanish bank where it maintains a bank account. During the same year, PAJ announced that it had plans to expand to the Spanish adult gaming market, as the latter was expected to grow annually by over 10%. As a result, PAJ started negotiations with local distributors and some (non-binding) memoranda of understanding have been signed.

However, like many other toy businesses, PAJ has faced the challenges of increased fixed costs and it has underestimated competition with web-based companies and an increasing preference for video games. For a few years now, PAJ has been beset by financial difficulties and, having witnessed the ongoing demise in revenue and fall in profits, it decided to file a petition to open safeguard proceedings (*procédure de sauvegarde*) in France. The petition was filed with the Strasbourg Court on 23 June 2017.

Assume that the EIR 2000 applies. Does the Strasbourg Court have international jurisdiction to open the requested insolvency proceeding? (Explain why it does or does not have jurisdiction.)

For commentary and feedback on self-assessment exercise 6, please see APPENDIX A

If the EU Insolvency Regulation does not apply and insolvency judgments are made in a jurisdiction that does not have a treaty with France, they are not automatically recognised. Foreign judgments can only be enforced if they have been subject to an *inter partes* procedure known as *exequatur*. If the judgment does not have *exequatur*, the French court can, first, open insolvency proceedings against the debtor company as long as the foreign judgment has not received *exequatur* in France.[147] Second, if the foreign judgment is not granted *exequatur*, the debtor needs to be considered as being *in bonis*, that is, in good standing in France. This means that the debtor is not deprived of the administration and disposal of their affairs and assets and is still liable to be pursued.[148]

In order for a foreign judgment to be granted *exequatur*, two procedural conditions must be met. First, the judgment must be an enforceable decision in the sense of Article 509 of the French Civil Procedure Code. Such decision consists of "any intervention of the judge which produces effects with regard to or on property or obligations". Secondly, the opening of insolvency proceedings in France is an obstacle to the enforcement of the foreign judgement, the two decisions being mutually exclusive.[149] On the other hand, the pronouncement of insolvency in France against a debtor requested to pay a sum of money abroad does not prevent the *exequatur* of the foreign decision, which does not constitute in itself a measure of execution but only a prerequisite to the adoption of such measure on the French territory.[150]

The criteria for obtaining *exequatur* are the following:

(1) the foreign court that issued the decision must have been competent to do so;

(2) the foreign judgment must comply with international public policy;

[147] Cass Com., 11 April 1995, *BCCI Overseas* prec.
[148] Cass. Req., 29 August 1826: S. 1826, 2, 428; Cass. Civ., 26 June 1905, *Richer*: DP 1905, 1, 513; Cass. Com., 28 June 2016, no 14-10.415.
[149] Cass. Com., 11 April 1995, *BCCI Overseas*, prec.
[150] Paris, 4 July 1991: *JDI* 1992, 705.

(3) the judgment must have been fraud-free.[151]

The judicial tribunal is the competent court to hear exequatur requests.[152] The French court that is seized of a request for *exequatur* must first ensure that the foreign judge who issued the decision was competent to do so. In doing so, the court will ensure that:

(i) it did not itself have exclusive jurisdiction to settle the dispute that gave rise to the judgment;

(ii) the dispute is linked to the country where the foreign court was seized;

(iii) there has been no fraud committed by the plaintiff who seized the foreign court.[153]

The French court will then verify the compliance of the foreign decision with international public policy, stemming from French law, but also EU law and international law.[154] The last element to check before responding favourably to an *exequatur* request is the absence of fraudulent intention by the plaintiff.

As a result of Brexit, since 2021 the United Kingdom (UK) is no longer able to open insolvency proceedings on the basis of the EU Insolvency Regulation. Furthermore, insolvency proceedings initiated in the UK after this date are no longer automatically recognised in France under the EU Insolvency Regulation. As with any jurisdiction that does not have an insolvency treaty with France, the recognition of insolvency judgments made in the UK will now be subject to the *exequatur* process.

French courts follow the principle of unity of the debtor's estate (*universalité de patrimoine*). This means that the court that has jurisdiction to open insolvency proceedings also has jurisdiction over all of the company's assets, whether located in France or abroad. There are some exceptions for assets located in EU member states, which apply when secondary proceedings are opened with respect to a company's branch(es) operating in another EU member state.

France has not adopted the UNCITRAL Model Law on Cross-Border Insolvency (1997). It is party to only very few bilateral conventions.[155]

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[151] Civ. 1st, 20 February 2007, No 05-14.082; Civ. 1st, 29 January 2014, No 12-28.953; Civ. 1st, 17 December 2014, No 13-21.365.

[152] Judicial Organization Code, Art R.212-8(2).

[153] Civ. 1st, 6 February 1985, No 83-11.241.

[154] Civ. 1st, 15 January 2020, No18-24.261.

[155] France is party to France-Belgium, Convention of 8 July 1899; France-Italy, Convention of 3 June 1930; France-Monaco, Convention of 13 September 1950; and France-Austria, Convention of 27 February 1979.

Self-Assessment Exercise 7 (Recognition of Foreign Judgments)

Question 1

When is it necessary to request the *exequatur* of a foreign judgment?

Question 2

What are the criteria for obtaining *exequatur* in France?

For commentary and feedback on self-assessment exercise 7, please see APPENDIX A

8. INSOLVENCY LAW REFORM

There are no current or planned reforms that will impact the French insolvency regime. However, it is worth mentioning the very recent reforms that took place in 2021. Ordinance 2021-1193 was published in September 2021 and came into force on 1 October 2021 (the "2021 Ordinance"). It brought about a comprehensive reform of the country's insolvency and restructuring landscape. It substantially modified and enhanced French restructuring tools while harmonising French insolvency law with security law, which was amended by a separate ordinance on the same day.

The 2021 Ordinance strengthened existing mechanisms to detect and prevent French companies' difficulties in several ways, thus entrenching temporary measures enacted during the COVID-19 health crisis. In particular, the following should be noted:

- the mechanisms for the detection of difficulties were accelerated, alongside warning procedures (*procédures d'alerte*);

- the conciliation procedure was strengthened through the modification of the procedure allowing the debtor to obtain a stay on enforcement action and claims;

- the French government merged the accelerated financial safeguard and the accelerated safeguard. The accelerated safeguard, combined with the conciliation procedure, are the reference framework for preventive measures in France, which implements the provisions of the EU Directive on Preventive Restructuring 2019;

- creditors' classes have replaced the previous committees of creditors. The creation of classes can be coupled with the ability to cross-class cram-down some creditors. Classes of affected parties are now mandatory and automatic under the accelerated safeguard procedure and subject to certain thresholds under the regular safeguard procedure;

- the provision for the separation into two distinct classes of secured creditors benefitting from rights *in rem* security interests and other creditors, as well as the constitution of one or more classes of equity holders (where applicable, if they are affected by the draft plan). The 2021 Ordinance also ensured that the distribution into classes would take into account subordination agreements entered into before the opening of the proceedings;

- the maximum duration of regular safeguard proceedings has been reduced to 12 months; and

- in rehabilitation proceedings, in the case creditors' classes are constituted, an impaired party may propose an alternative draft restructuring plan.

The 2021 Ordinance entrenched aspects of security law into insolvency law in line with the reform of the French security regime.[156]

9. USEFUL INFORMATION

9.1 Books

- N Borga *et al*, *Droit des entreprises en difficulté* (LexisNexis, 2022);

- A Donnette-Boissiere *et al*, *Entreprises en difficulté* (LGDJ, 2022);

- R Dammann and M Senechal, *Le droit de l'insolvabilité internationale* (Joly, 2018); and

- P Petel, *Procédures collectives* (Dalloz, 2021).

9.2 Articles

- E Ghio, "Transposing the preventive restructuring directive 2019 into French insolvency law: Rethinking the role of the judge and rebalancing creditors' rights", *International Insolvency Review* (2021) 30 54; and

- E Ghio and P Omar, "Mapping Preventive Restructuring Frameworks and the EU Directive for the JCOERE Project. Country Report: France", JCOERE Project (2020).

9.3 Online resources

- https://uk.practicallaw.thomsonreuters.com/1-501-6905?transitionType=Default&contextData=(sc.Default)&firstPage=true

- https://practiceguides.chambers.com/practice-guides/insolvency-2021/france;

[156] Ordinance n.2021-1192 of 15 September 2021 reforming security law.

- https://uk.practicallaw.thomsonreuters.com/1-501-6905?transitionType=Default&contextData=(sc.Default)&firstPage=true#co_anchor_a757392.

APPENDIX A: COMMENTARY AND FEEDBACK ON SELF-ASSESSMENT EXERCISES

Self-Assessment Exercise 1

Study the aspects dealt with in the previous section.

France has long been considered to be a debtor-oriented jurisdiction in relation to its insolvency regime. Outline the reasons why this view has come to prevail and explain how this is, or is not, relevant nowadays.

Commentary and Feedback on Self-Assessment Exercise 1

The first French pre-insolvency process was introduced as early as 1984. Since then, the French legislator and government have been exceptionally prolific in regularly modernising the French preventive restructuring landscape, with substantial reforms occurring every couple of years. This continuous reform activity is partly a reaction to regular economic crises, which have led to an increase in the number of insolvency cases, and partly to the consideration that previous reforms had fallen short of success. Over the years, most reform efforts have centred around the acknowledgement that the more the difficulties of the company are dealt with upstream, the better the chances are of preserving the value of the assets of the company and to achieve a successful restructuring. As a result, the French preventive restructuring regime geared towards promoting the rescue of businesses at an early stage, with a view to preserving employment. It is a comprehensive body of law, with no less than five corporate rescue procedures:

1. *ad hoc* mandate (*mandat ad hoc*);
2. conciliation (*conciliation*);
3. safeguard (*sauvegarde*);
4. accelerated safeguard (*sauvegarde accélérée*); and
5. rehabilitation procedure (*redressement judiciaire*).

Additionally, in comparison to other jurisdictions, French insolvency law is unusual for its rather low level of involvement of creditors and the protection afforded to their interests compared to those of other stakeholders. As a result, the French regime ranks quite low in international studies, which often rely predominantly on the role of creditors in insolvency procedures, as well as their recovery rates. It is, therefore, not surprising that commentators have branded France as "bias[ed] in favour of both the management of the failing business and its shareholders" and called for rebalancing the protection afforded to creditors.

Self-Assessment Exercise 2

Study the aspects dealt with in the previous section.

Under French law, a secured creditor can enforce a mortgage in three different ways. Outline these possibilities.

Commentary and feedback on Self-Assessment Exercise 2

In relation to the enforcement of a mortgage, secured creditors have three possibilities:

- The beneficiary of a mortgage may apply to the court for an order to seize the property (*commandement aux fins de saisie*) to be served on the debtor by a bailiff (*huissier de justice*). Following the proceedings to be carried out in accordance with Articles L311-1 *et seq* and R311-1 *et seq* of the Civil Enforcement Proceedings Code (*Code des procedures civiles d'exécution*), the property is sold by way of public auction at a hearing before the court (*tribunal judiciaire*), where bidders must be represented by a legal representative who cannot bid and neither can the creditor.
- The beneficiary of a mortgage may also apply to court for the attribution of a court order of the property to the beneficiary of the mortgage, in accordance with a court-monitored allocation process (*attribution judiciaire*) pursuant to Article 2458 of the French Civil Code. This option is not available to the creditor if the property is the main residence of the debtor.
- Pursuant to Article 2459 of the French Civil Code, it may be agreed in the mortgage deed that the creditor is to become the owner of the mortgaged property (*pacte commissoire*). In this case, the value of the property is determined on the day of the transfer by an expert designated by the parties, or judicially if no agreement can be reached. This clause is, however, ineffective if the property is the main residence of the debtor.

Self-Assessment Exercise 3

Study the aspects dealt with in section 6.2 on personal bankruptcy.

Look at the personal recovery procedure (*rétablissement personnel*). Two types of personal recovery procedures exist. What are they and what are their purposes and differences?

Commentary and Feedback on Self-Assessment Exercise 3

When the debtor is in an irremediably compromised situation characterised by the apparent impossibility of implementing rehabilitative measures, the bankruptcy commission has two options. It can firstly recommend a recovery without judicial liquidation if it finds that the debtor only has movable property necessary for everyday life and non-professional property essential for the exercise of their professional activity, or that the assets consist only of valueless property or whose selling costs are disproportionate to their market value. Secondly, it can also, if it finds that the debtor is not in the previous situation, and with the agreement of the debtor, seize the judge for the purpose of opening a personal recovery procedure with judicial liquidation (Consumer Code, Article L724-1).

Personal recovery without judicial liquidation: The debtor must not have any seizable assets and therefore this procedure can only be used if the debtor either has nothing, or has only movable property necessary for their daily life, or non-professional property but essential for the exercise of their professional activity, or has goods of little market value or whose selling costs would be manifestly disproportionate to their market value. The debtor's agreement is not expressly required in this procedure. When the commission decides to open a procedure of personal recovery without judicial liquidation, it informs the parties by registered letter with acknowledgment of receipt, indicating that they can contest the choice made by the commission. They must inform the court within fifteen days (Consumer Code, Article L332-5-1). The commission then communicates its recommendation to the judge. If no dispute has been raised within fifteen days, the judge verifies that the procedure is well-founded (Consumer Code, Article R334-21). The judge then sanctions the commission's decision which is also published in the BODACC.

Personal recovery with judicial liquidation: the debtor's consent is necessary due to the serious nature of the procedure that ends with judicial liquidation and severely affects the assets of the debtor. The procedure is only possible if the debtor has seizable assets since, in the opposite case, the Consumer Code provides for recourse to the other (non-liquidation) procedure (Consumer Code, Article L330-1). The opening of a personal recovery with judicial liquidation entails the suspension of legal proceedings in the course of execution of the procedure, including expulsion measures. This stay lasts until the closing judgment (Consumer Code, Article L332-6). Once seized, the court organises a hearing where the debtor and their creditors are summoned (Consumer Code, Article L332-6; Article R334-31). As of the opening of the judgment, the debtor may no longer dispose of its property. To alienate them, it must obtain the agreement of the court. Additionally, the debtor cannot worsen its financial situation, at the risk of seeing the procedure terminated (Consumer Code, Article L333-2). In this respect, the debtor does not have the right to pay claims which arose before the opening judgment (Consumer Code, Article L331-3-1). Depending on the situation of the debtor, the judge will decide on the most appropriate measures to put an end to its insolvency (Consumer Code, Article R334-40). The appointed liquidator must manage the debtor's assets and liquidate the assets in order to be able to settle the liabilities.

Self-Assessment Exercise 4

Study the aspects dealt with in the previous section.

Consider the timeline of liquidation proceedings. The liquidation procedure is not constrained by any legal timeframe, except in the case of simplified liquidation proceedings in which case, its duration cannot exceed twelve months (which can be exceptionally extended by three months). In your opinion, why is it beneficial for liquidation proceedings to be as speedy as possible?

Commentary and Feedback on Self-Assessment Exercise 4

The procedure of simplified liquidation, created by the Law of 26 July 2005, aims at accelerating the course of liquidation proceedings. It only applies to debtors who have no real estate assets and if the company does not exceed certain fairly low thresholds. However, the Pacte Law of 22 May 2019 aimed at increasing the effectiveness of the simplified liquidation procedure. It made the procedure mandatory below certain thresholds set by the decree of 21 November 2019. This amendment targeted small and medium-sized enterprises, employing a maximum of five employees and generating less than EUR 750,000 in turnover.

The uniqueness of the procedure lies in the realisation of the assets of the company which are sold at public auction, or directly to third parties, by the liquidator within three months following the judgment opening liquidation proceedings. The procedure is also streamlined in the sense that debts that have no chance of being paid off, especially unsecured debts, are not verified. Only claims arising from an employment contract or those likely to be paid (as they are of so-called useful rank), are eligible.

While the law does not provide for a maximum duration for regular liquidation proceedings, it establishes, on the other hand, a legal limit for simplified liquidation proceedings: its duration cannot exceed twelve months, but can be extended by three months under exceptional circumstances.

Overall, the simplified procedure is similar to the regular procedure but provides more flexibility and constrains the proceedings to a limited timeframe.

Self-Assessment Exercise 5

Study the aspects dealt with in the previous section.

Question 1

Consider the preventive reference framework that is the combination of conciliation proceedings with accelerated safeguard proceedings. This framework is considered to be a pre-pack option for distressed debtors. Outline how this framework works and the specific features attached to both the conciliation phase and the accelerated safeguard phase.

Question 2

While the safeguard procedure and rehabilitation process exhibit many similarities, recent reforms have sharpened their differences. What are the main differences between the safeguard and the rehabilitation procedures?

Commentary and Feedback on Self-Assessment 5

Question 1

The accelerated safeguard is not a standalone procedure. It must be preceded by a conciliation process. Article L628-1 of the Commercial Code provides that the accelerated safeguard procedure is opened at the request of a debtor engaged in a procedure of conciliation. The conciliation procedure must be ongoing when accelerated safeguard proceedings are launched. Article L628-2 indicates that the court decides, after a report from the conciliator, whether or not to open accelerated safeguard proceedings. The criteria for opening accelerated safeguard proceedings are that:

- the debtor be engaged in conciliation proceedings; and
- a plan has been drafted during the conciliation phase which is likely to be adopted within three months from the opening judgment by the creditors impacted by the plan (Commercial Code, Article L628-8).

The accelerated safeguard procedure remains subject to most of the rules of the regular safeguard procedure.

The procedure is opened at the request of the debtor. The court may appoint one or more judicial administrators. The opening of the procedure is subject to the constitution of creditors' classes, as per Article L626-29 of the Commercial Code.

The court has three months, from the opening judgment, to approve the plan under the conditions provided for in Article L626-31. Within this short period, it is necessary to have set up and convened the classes of creditors, credit institutions and suppliers and, where applicable, the meeting of bondholders. In sanctioning the plan, the court must ensure that it preserves the interests of all creditors. In practice, this requires that the plan be prepared upstream during the conciliation phase, and adopted by a majority, its decision binding the minority. Cross-class cram-down and associated safeguard rules apply to accelerated safeguard.

Importantly, creditors benefit from a new money privilege. In order to encourage creditors to finance the restructuring, Article L611-11 of the Commercial Code grants priority of payment to persons who provides, within the framework of a conciliation procedure, a new cash contribution to the debtor in order to ensure the continuation of the activity of the company and its sustainability; as well as to those who provide new goods or services in order to ensure the continuation of the activity of the company and its sustainability. These claims will take precedence over other creditors in case of subsequent rescue or liquidation proceedings.

Question 2

Overall, the two procedures are relatively similar, especially with the opening of the observation period and the processes surrounding the plan. The roles of stakeholders are the same and so are most of the legal rules.

Nonetheless, the safeguard procedure was intended by the legislator as a pre-insolvency mechanism. The company cannot be insolvent to avail of safeguard proceedings, which is not the case with rehabilitation proceedings. Therefore, the absence of a payment failure situation is the main axis of the difference between the safeguard and the rehabilitation procedures.

As a way to further encourage debtors to tackle financial difficulties at an early stage, the law now provides for a number of changes which make safeguard or more debtor-driven, pre-insolvency procedure in comparison to rehabilitation proceedings. The main differences are:

- creditor participation: where classes are constituted in rehabilitation proceedings, a party impaired by the plan can propose an alternative plan to be voted on in competition with the debtor's plan. A creditor can also petition the court to exercise its power to order cross-class cram-down. The safeguard procedure only permits the debtor to propose a plan and / or cross-class cram-down; and
- the maximum duration of the safeguard procedure is now 12 months (six months renewable once), while rehabilitation proceedings can last for up to 18 months.

Self-Assessment Exercise 6 (Cross-Border Insolvency)

Prêt A Jouer (PAJ) is a France-registered toy shop company. The company opened its first store in Strasbourg in 2011. One of PAJ's warehouses is in Madrid (Spain) and PAJ rents out this warehouse to other toy companies. In 2013, PAJ concluded a line of credit agreement with a Spanish bank where it maintains a bank account. During the same year, PAJ announced that it had plans to expand to the Spanish adult gaming market, as the latter was expected to grow annually by over 10%. As a result, PAJ started negotiations with local distributors and some (non-binding) memoranda of understanding have been signed.

However, like many other toy businesses, PAJ has faced the challenges of increased fixed costs and it has underestimated competition with web-based companies and an increasing preference for video games. For a few years now, PAJ has been beset by financial difficulties and, having witnessed the ongoing demise in revenue and fall in profits, it decided to file a petition to open safeguard proceedings (*procédure de sauvegarde*) in France. The petition was filed with the Strasbourg Court on 23 June 2017.

Assume that the EIR 2000 applies. Does the Strasbourg Court have international jurisdiction to open the requested insolvency proceeding? (Explain why it does or does not have jurisdiction.)

Commentary and Feedback on Self-Assessment 6

- The Strasbourg Court has international insolvency jurisdiction to open insolvency proceedings against PAJ.
- Under both the EIR Recast (Article 3) and the EIR 2000 (Article 3), the determination of international jurisdiction to open main insolvency proceedings is linked to the debtor's centre of main interest (COMI). According to Article 3 EIR Recast, COMI shall be the place where the debtor conducts the administration of its interests on a regular basis and which is ascertainable by third parties (see also Recital 28). In the EIR 2000, similar statement was only provided in a recital (Recital 13). In the case of a company, the place of the registered office shall be presumed to be the COMI in the absence of proof to the contrary.
- Relevant case law: *Eurofood IFSC Ltd*, Case C-341/04, ECLI:EU:C:2006:281 (May 2, 2006) and *Interedil Srl, in liquidation v Fallimento Interedil Srl*, Case C-396/09, ECLI:EU:C:2011:671 (Oct. 20, 2011).
- PAJ is registered in France and operates from there. The fact that PAJ owns some assets (i.e. warehouse) in Spain and has entered into contracts for the financial exploitation of those assets cannot be regarded as sufficient factors to rebut the presumption laid down in Article 3(1) (see para. 52 in *Interedil*).
- The plans to expand to the Spanish toy and gaming market and ongoing negotiations with local distributors (with whom some non-binding memorandums of understanding have been signed) also cannot rebut the strong presumption in favour of the jurisdiction of the registered office, which resulted from the *Eurofood* judgement. Besides, it must have been obvious to such local distributors that the debtor conducted the administration of its interests from France (actual centre of management) and it did so on a regular basis, since PAJ's Spanish presence was rather incidental, marginal and limited in time and purpose.

Self-Assessment Exercise 7 (Recognition of Foreign Judgments)

Question 1

When is it necessary to request the *exequatur* of a foreign judgment?

Question 2

What are the criteria for obtaining *exequatur* in France?

Commentary and Feedback on Self-Assessment Exercise 7

Question 1

It is necessary to have recourse to an exequatur procedure in France when a foreign debtor has assets in France. If a foreign judgment produces a certain number of effects in France, its enforcement can only take place if it is recognised and enforceable, which implies the granting of exequatur by the French court. Without exequatur, the foreign judgment cannot be enforced against the debtor located on French territory.

In the absence of exequatur, the debtor will be considered to be *in bonis* in France. As a result, they are not deprived of the management and disposal of their assets and may be subject to individual proceedings by creditors in France.

Additionally, in the absence of an exequatur, a foreign insolvency practitioner will not be able to enforce the decision on the assets of the debtor located in France.

Question 2

The French court who is seized of a request for exequatur must first ensure that the foreign judge who issued the decision was competent to do so. In doing so, the court will ensure that:

- it did not itself have exclusive jurisdiction to settle the dispute that gave rise to the judgment;
- the dispute is linked to the country where the foreign court was seized;
- there has been no fraud committed by the plaintiff who seized the foreign court.[157]

[157] Civ. 1st, 6 February 1985, No 83-11.241.

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