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ARTICLE

Secondary Insolvency Proceedings in France: Potential Liability of Directors of Foreign Companies for Insufficiency of Assets in France

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I. The principle of universality in cross-border insolvency proceedings under EC Regulation No. 1346/2000 of 29 May 2000

EC Regulation No. 1346/2000 of 29 May 2000 on insolvency proceedings (the 'Insolvency Regulation') is a foundation text which aims to allow the efficient operation of cross-border insolvency proceedings in Europe.

The Insolvency Regulation, a practical example of the principle of judicial cooperation in relation to insolvency procedures, had become a real necessity in order to regulate potential conflicts of law as well as practical problems caused by overlapping national regulations in the different Member States. At a more global level, the Insolvency Regulation was also required to streamline cross-border insolvency proceedings to avoid them, to the extent possible, disrupting the proper and effective functioning of the internal market.

In practice, the different parties involved in cross border proceedings would regularly come up against conflicts of laws, some of which would be more favourable to creditors whilst others would be more favourable to debtors or employees. In addition, practitioners would often be faced with problems relating to protective legal measures having been taken in relation to assets of the debtor in other Member States to the one in which the main proceedings had been commenced.

Obstacles such as the ones outlined above inevitably led to debtors forum shopping in an attempt to move their centre of main interests (COMI) to a Member State with more favourable legislation. This ultimately made the liquidation of a debtor company's assets complicated to carry out to the detriment of having fairly balanced proceedings and equality amongst creditors.

In this context, the principle represented by the Insolvency Regulation has sought to bring some clarity to the problem. Accordingly, subject to specific rules which relate to certain overriding issues in each state (such as in respect of property, employment law etc), the insolvency proceedings opened in the Member State in which the debtor has its COMI will have universal application and be fully recognised by all other Member States.

In other words, this procedure enables the liquidator designated in the main proceedings to take all measures in relation to all the assets of the debtor irrespective of the Member States in which such assets may be located and, in relation to questions of liability, to take any action against any directors who may be at fault.

As a corollary of this principle, if secondary liquidation proceedings are commenced in one or more other Member States in which the debtor may have a place of business, the effects of such secondary proceedings and the measures which may be taken by the liquidator will be limited to assets located in the Member State or States in question.

In this context, it is relevant to consider how the courts have dealt with the application of these principles in relation to directors' liability.

II. A restrictive application of the Insolvency Regulation by both European and French courts

In the renowned *Gourdain* judgment,[1] the Court of Justice of the European Union held that the former *comblement de passif* action (making good liabilities – now replaced by the liability for insufficiency of assets) fell within the jurisdiction of the courts of the Member State in which the insolvency proceedings had been commenced given that such courts had knowledge of 'all actions which originate directly from the insolvency proceedings and which are closely connected to them'. The Court therefore adopted a strict interpretation of the principle of *vis attractiva concursus*.

The French Supreme Court (*La Cour de Cassation*)[2] has followed the judicial rationale adopted in the *Gourdain* case up until now and has held that the court before which secondary proceedings have been commenced in

Notes

1 Case 133/78 – Judgment of the Court of 22 February 1979. – *Henri Gourdain v Franz Nadler.*

2 Cass. Com – Case number 11-17.968 – 22 January 2013.

France is not competent to impose any sanction in respect of any insufficiency of assets nor any prohibition on carrying out management functions. The Supreme Court has accordingly granted exclusive jurisdiction to the court handling the main proceedings in respect of imposing sanctions on directors by relying on the following two principles:

– on the one hand, it is not possible to bring an action relating to sanctions within the framework of secondary proceedings (which is a consequence of the specific – as opposed to universal – nature of such proceedings);
– on the other hand, actions relating to sanctions are included within the scope of the main insolvency proceedings (being a direct consequence of the general and universal nature of such proceedings).

In France, this interpretation has led to a regime where no liability will be attributed to any directors in the event that secondary proceedings are commenced. Whilst it is possible to understand that this outcome is within the spirit of the Insolvency Regulation and in particular reflects the concern of European legislators to avoid directors being prosecuted in several jurisdictions for the same faults, it cannot be excluded that if the liquidator in the main proceedings does not cooperate with those in charge of the secondary proceedings (which in practice is often the case) and decides not to prosecute a director for his fault, such director may slip through the net and avoid liability altogether.

III. The Judgment of the Commercial Court of Nanterre (*Tribunal de Commerce de Nanterre*) dated 13 November 2013 now opens a new avenue for holding foreign directors liable

In a judgment dated 13 November 2013, the Commercial Court of Nanterre held that it was competent to rule upon whether the legal and *de facto* directors of a company were liable for damages within the scope of secondary proceedings commenced in France regarding insufficiency of assets in accordance with the provisions of article L.651-2 of the French Commercial Code.

In this case, the Court of Munich had, pursuant to a judgment dated 20 June 2011, commenced main insolvency proceedings against a German company called Alkor which had two places of business (establishments)[3] in France.

Subsequent to the main proceedings being initiated in Germany, the Commercial Court of Nanterre, at the request of the German liquidator, opened secondary proceedings regarding the two French places of business on 8 July 2011.

The liquidator in the secondary proceedings sought a judgment from the Commercial Court of Nanterre regarding the liability of the directors of Alkor to pay damages in respect of the insufficiency of assets pursuant to article L651-2 of the French Commercial Code. The liquidator also brought an action against an investment fund called GB Europe which had granted the company a credit line of EUR 10 million on ruinous terms on the basis that such fund had acted as a *de facto* director.

Contrary to the position previously adopted by the Court of Justice of the European Union, the Commercial Court of Nanterre justified its position by stating that 'the jurisdiction of the Court was not strictly limited to the realisation of assets in the strict sense of the term, meaning realising assets located in the French territory and dealing with the liabilities declared in the proceedings, but also included any actions inseparable from the judicial liquidation proceedings'.

Indeed, according to the Commercial Court of Nanterre, even where main proceedings have been commenced, the courts dealing with the secondary proceedings retain the power to exercise the rights which are conferred on them under the applicable national law save for those exceptions provided for under the Insolvency Regulation. The Insolvency Regulation does not provide for any exception in relation to sanctions. Therefore, in principle, nothing prevents the judge in charge of the secondary proceedings from applying the sanctions regime provided for under the relevant national law. This analysis, which is contrary to the jurisprudence initiated by *Gourdain*, is attractive in that it suggests a possible way to sanction legal or *de facto* directors for wrongful acts, especially where the latter would not otherwise fall within the power to sanction of the French courts.

Accordingly, the Commercial Court of Nanterre has once again demonstrated its willingness to adopt pragmatic and innovative solutions amounting to a broad application of the Insolvency Regulation.

However, it should be stressed that in the case at hand, the secondary character of the proceedings initiated before the Commercial Court of Nanterre has been challenged by one of the directors of the German company to the extent that the proceedings initiated in Germany, considered as the main proceedings, were only temporary.

Therefore, the judgment against the directors of the German company still remains subject to the confirmation of the secondary nature of the insolvency proceedings opened by the Commercial Court

Notes

3 '[A]ny place of operations where the debtor carries out a non-transitory economic activity with human means and goods' Article 2(h) Insolvency Regulation.

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of Nanterre, which means meeting the requirements of article L651-2 of the French Commercial Code: the opening of a judicial liquidation procedure in France.

In that respect, a French Court of Appeal has already rejected the appeal by the German director and a further judicial recourse has been initiated. The Commercial Court of Nanterre has accordingly stayed the proceedings pending the final decision of the French Courts.

The last step towards the recognition of the possibility of holding a director liable within the context of secondary insolvency proceedings is perhaps, therefore, about to be taken.

In view of this, practitioners will need to find means to ensure that directors of companies which have subsidiaries or establishments in France are adequately protected. In particular this may include erecting legal barriers such as the granting of delegations of powers, the appointment of local directors etc. In any event, innovative remedies will need to be devised as a defence to the cutting-edge approach of French courts!

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