

Coeur Défense: what's new?

An update of the landmark case after the recent decision of the *Cour de Cassation*

On 8 March 2011, the *Cour de Cassation*, the French Supreme Court, has quashed the decisions dated 25 February 2010 of the Paris Court of Appeal that had nullified the opening of safeguard proceedings in relation to Heart of La Défense SAS ("**Hold SAS**") and its sole shareholder Sàrl Dame Luxembourg ("**Dame Lux**").

The safeguard proceedings of these two companies, which were initiated in November 2008, are therefore reinstated. However, another litigation, initiated by the appeal of the Public Prosecutor against the safeguard plan restructuring the debts of Hold SAS and Dame Lux, is still pending and will now be heard by the Paris Court of Appeal.

Background

Hold SAS a special purpose vehicle, borrowed EUR 1.64 billion under a property financing secured on the Coeur Défense complex in the Paris district of La Défense extended by Lehman Brothers. Dame Lux is its Luxembourg parent and had provided a limited recourse share pledge ("*cautionnement réel*") to secure the debt. The EUR 1.64 billion indebtedness was subsequently securitized through the issue of commercial mortgaged-backed securities (CMBS) by the *Fonds Commun de Titrisation* Windermere XII FCT represented by Eurotitrisation.

By two decisions dated 25 February 2010, the Paris Court of Appeal had annulled the opening of the safeguard proceedings. The decision of the Paris Court of Appeal had been interpreted as a sign that French courts would now tend to refuse the opening of safeguard proceedings whose sole purpose would be to impose a debt restructuring favouring the interests of equity investors. However, certain commentators had criticized the Paris Court of Appeal's reasoning, and this decision has been interpreted as being in contradiction with the latest legislative reforms, which clearly aim at encouraging debtors to use safeguard proceedings at an early stage of their difficulties.

The core test for the opening of safeguard proceedings

In its decision of 8 March 2011, the *Cour de Cassation* mainly focused on the core test for the opening of safeguard proceedings set out under article L.620-1 of the *Code de Commerce* and pointed out that the sole condition for a company to benefit from such proceedings consists in its ability to demonstrate that it is facing difficulties that it cannot overcome (at the time of the judgment the test also included that these difficulties were of a nature to lead to cessation of payments).

SUMMARY

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The *Cour de Cassation* held that the Paris Court of Appeal, by referring to the "core activity" of the company, had added a new condition to the test for the opening of safeguard proceedings that was not in the *Code de Commerce*. In particular, and even though the purpose of safeguard proceedings is to enable the company to pursue its economic activity, the fact that the difficulties faced by such company are directly or indirectly related to its core activity is considered irrelevant for the purpose of such test.

Similarly, the fact that a change of the shareholding control by reason of the enforcement of the share pledge granted by Dame Lux does not affect the ability of Hold SAS to pursue its economic activity (i.e. the leasing of its building) does not in itself constitute according to the *Cour de Cassation* a legitimate ground to annul the opening of safeguard proceedings.

Insurmountable difficulties

The Paris Court of Appeal had concluded that the obligation to replace a hedging arrangement at greater cost was not in itself a sufficient reason to permit the company to petition for the commencement safeguard proceedings, with regard in particular to the global and initial balance of the transaction. The *Cour de Cassation* ruled out this conclusion on the basis of the statement by Hold SAS that it was impossible in October 2008 to find a new hedging counterparty and, as a result, that the replacement costs were not only insurmountable but also purely theoretical.

Besides the Paris Court of Appeal had held that the sole consequence of the default of Hold SAS under the loan would be the loss by Dame Lux of its investment as a result of the enforcement of the pledge over the shares it holds in its subsidiary. No other liability was validly evidenced by Dame Lux. The *Cour de Cassation* did not contest in its judgment that the guarantee granted by Dame Lux was other than of a limited recourse nature which would be fully discharged upon enforcement of the pledge. However, the conclusion of the Paris Court of Appeal is rejected on the ground that shareholder loans, which have been validly evidenced through the books of the company, constituted significant liabilities of Dame Lux that it, deprived of its sole asset by reason of the breach by Hold SAS of its contractual obligations, would not be in a position to face.

Appeals against judgments opening safeguard proceedings

Finally, the *Cour de Cassation* in its judgment confirms the decision of the Paris Court of Appeal whereby a creditor is entitled to appeal against a judgment opening safeguard proceedings, provided such creditor has a personal and legitimate interest which is different from the interest of the collectivity of the creditors. In the case at hand, the *Cour de Cassation* has confirmed that Windermere XII FCT had a personal interest to appeal against the judgments opening the safeguard proceedings of Hold SAS and Dame Lux. This position of the *Cour de Cassation* therefore opens the floodgates for appeals by creditors against judgments opening safeguard proceedings if such creditors can demonstrate that the conditions for the opening of safeguard proceedings were not met.

Next steps

In accordance with French procedural rules, the case is now going to be tried again, before the Versailles Court of Appeal. Considering the judgment of the *Cour de Cassation*, the FCT will need to convince the court that Hold SAS and Dame Lux were not facing insurmountable difficulties when the safeguard proceedings were opened.

In addition, another litigation is still pending regarding the safeguard plan restructuring the debts of Hold SAS and Dame Lux that was adopted by the Paris Commercial Court on 9 September 2009. The Public Prosecutor and the FCT had decided to challenge the plan on the ground that it did not comply with certain mandatory rules that are meant to protect creditors. The reinstatement of the safeguard proceedings also results in the reinstatement of this litigation.

This Client briefing does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

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