

FRENCH SUPREME COURT FINDS ROMANIAN INSOLVENCY PROCEEDINGS PROTECT DIRECTOR FROM SANCTIONS IN FRANCE ARISING FROM MANDATORY FILING OBLIGATIONS

INTRODUCTION

In formal insolvency situations in most places around the globe, management can find themselves subject to the scrutiny of insolvency officeholders; who investigate and consider the cause of the failure. Obligations in the period immediately before a formal process is commenced can be very strict, in some jurisdictions management are left with little time to consider restructuring options and instead are subject to a mandatory time period which obliges them to commence a formal process. The consequences of failing to file can be severe and can include personal liability, prohibitions on management, and in some cases criminal sanctions. (See our summary table for mandatory time limits and potential liabilities below.)

A recent French Supreme Court Case (M.X as liquidator of Izoplac v MY [2018 I. L. Pr 24]) may offer some comfort where more than one court in the EU commences proceedings against the same debtor, as the management can rely upon the formal filing made in one jurisdiction to satisfy its obligation to file according to the law in another Member State. In this case the original insolvency proceedings in Romania were opened some two years prior to proceedings being commenced in France. The Supreme Court held that the French proceedings were secondary proceedings and the filing of the Romanian proceedings meant that the director based in France could not be sanctioned for not having filed in France after the commencement of main proceedings in Romania. It may be worth noting that the Romanian court did not articulate in opening the proceedings that they were main proceedings. Since 26 June 2017 there has been a requirement under the European Insolvency Regulation (Recast) (Recast Regulation) (Article 4) that the court commencing the proceedings must specify whether they are main, secondary, or territorial proceedings (see box below for a summary of the key concepts in the Recast Regulation). There is also a new recital in the Recast Regulation (para 47) which expressly opens the door for "the courts of a Member State in which secondary insolvency proceedings have been opened [to sanction] a debtor's directors for violation of their duties, provided that those courts have jurisdiction to address such disputes under their national law". Accordingly, directors could still be pursued in more than one jurisdiction, on other grounds than those at stake in the case.

Key issues

- Romanian insolvency proceedings
- Recast Insolvency Regulation means automatic recognition of main insolvency proceedings across the EU
- Proceedings opened later in France were secondary proceedings
- French court's decision to ban director for failure to file in France within 45 days overturned by French Supreme Court
- Romanian proceedings protected the French director from mandatory filing requirements in France

Although the effect of this decision is limited to France – it is reassuring to note that the effects of the automatic recognition and effect of main proceedings under the European Insolvency Regulation (the predecessor to the Recast Regulation) mean that a director can be relieved of these often perceived onerous mandatory filing requirements. This is not the first time this issue has been considered in a cross border insolvency case, the German courts took a similar approach in *Collins & Aikman*. Increasingly as businesses became more international – the principle of recognition and effect under the EUIR is a very useful confirmation, not least because it may avoid multiple proceedings being commenced in the first place. This latest French decision may offer reassurance to those operating in France and elsewhere.

From 26 June 2018 each EU Member State became obliged to establish and maintain an Insolvency Register pursuant to the Recast Regulation. This may have deterred the French courts, or at least put them on notice, that there were proceedings already afoot in Romania for the same company.

Of course, from the UK's perspective, unless there is an equivalent regime in the EU after Brexit, English insolvency proceedings will not be automatically recognised elsewhere, so a formal application for recognition may be required. This asymmetry is not ideal, and may result in additional time and costs for cross border cases involving UK proceedings. Of course, the Recast Regulation will continue to operate in favour of EU proceedings throughout the EU and in the UK as the UK will adopt the Recast Regulation in accordance with the European Union (Withdrawal) Act 2018.

TIME LINE

- 27 June 2012 Romanian court opens insolvency proceedings in respect of Izoplac.
- 19 March 2014 French commercial court in Créteil opens a French liquidation process of Izoplac. Fixes 12 September 2012 as date it became unable to pay its debts.
- 3 Nov 2016 French Court of Appeal: director prohibited from managing company for one year due to failure to file for insolvency in France within 45 days of becoming unable to pay its debts.
- 7 Feb 2018 French Supreme Court quashed the Court of Appeal's decision.

RESTRUCTURING AND INSOLVENCY TRENDS IN EUROPE

Time limits for filing for insolvency					
England & Wales	France	Germany	Italy	Spain	The Netherlands
No express time limit Failure to take action which results in a loss may give rise to action against directors personally	Obligation to file for either a judicial rehabilitation or liquidation proceeding within 45 days of cash-flow insolvency (except if a conciliation proceeding has been filed for)	Obligation to file immediately when unable to pay debts or over indebtedness. Filing may be postponed for up to 21 days if reasonable expectations exist that insolvency can be overcome	No express time limit Failure to take action which results in a loss may give rise to action against directors personally	Obligation to file within 2 months of insolvency. Failure to comply assumes that bankruptcy is carried out negligently	No express time limit Failure to take action which results in a loss may give rise to action against directors personally
Types of liability for directors in an insolvency					
For breaches of duties, wrongful trading and fraudulent trading	For cases of mismanagement that has contributed to the deficiency of assets of the debtor or to the insolvency of the debtor (e.g. late filing for insolvency proceedings)	For failure to file for insolvency, for any payments made to third parties after the company becomes insolvent and for any new agreements which the company is unable to fulfil	For breaches of duty and failure to preserve the company's value if that failure results in a loss to creditors. Criminal liability for directors who either: (i) distracted, disguised or voluntarily lost the assets; (ii) delayed the declaration of bankruptcy; or (iii) disguised the company's financial distress or its insolvency state in order to obtain financing	For case where insolvency is considered as negligent, and where directors have contributed to the insolvency	For mismanagement, wrongful distribution, fraud or if the directors have contributed to provoke the company's insolvency

The European Regulation on Insolvency Proceedings (Recast) (the Recast Regulation)

Overview

The Recast Regulation does not provide uniform substantive legal provisions for members of the EU. It codifies how a Member State should determine whether it has jurisdiction to open insolvency proceedings, whilst also imposing a uniform approach to the governing law applicable to those proceedings. The Recast Regulation also provides for the automatic recognition of insolvency proceedings throughout the EU. Once these factors have been determined, the procedural rules of the Member State in which proceedings are opened will generally apply.

Scope

The Recast Regulation applies to all collective insolvency proceedings relating to corporate entities and individuals within the EU. An exhaustive list of the types of proceedings is set out in Annex A of the Recast Regulation for each Member State. From 26 June 2017 secondary proceedings under the Recast Regulation are no longer limited to winding up proceedings. The scope of its application is confined to parties with their centre of main interests within a Member State of the EU. It does not apply to banks, credit institutions, insurance companies, investment undertakings which hold funds or securities for third parties, or collective investment schemes, which benefit from different EU legislative instruments.

Jurisdiction

The primary jurisdiction for insolvency proceedings, as provided by the Recast Regulation, is the court of the Member State where the debtor's centre of main interests (COMI) is located. In the case of a company or other legal person, in the absence of proof to the contrary, there is a rebuttable presumption that the COMI is in the Member State where the registered office of the company or other legal person is located.

The Recast Regulation allows for the courts in countries to open "territorial" insolvency proceedings or, after the commencement of main proceedings, "secondary" proceedings, in the event that such debtor possesses an establishment in the territory of such other Member State. The applicable law of such territorial or secondary insolvency proceedings will be the law of that other Member State.

Governing law (Article 7 of the Recast Regulation)

The Recast Regulation imposes a unified code for the governing law. The general rule is that the law applicable to the insolvency proceedings and its effects shall be that of the Member State within the territory in which such proceedings are opened.

Exceptions to the governing law (Articles 8 to 18 of the Recast Regulation)

The Recast Regulation recognises that there will be cases where strict adherence to the general rule on governing law will interfere with the rules under which transactions are carried out in other Member States, and therefore the general rule is subject to a number of exceptions and carve-outs.

These exceptions include '*rights in rem*' including, amongst other things, rights of security (Article 8) rights of set-off permitted by the law applicable to the insolvent debtor's claim (Article 9), rights under a reservation of title clause (Article 10), contracts relating to immovable property (Article 11), rules of payment systems and financial markets and contracts of employment (Article 12).

Establishment of Insolvency Registers (Article 24 of the Recast Regulation)

From 26 June 2018, each Member State is obliged to have established and maintain one or several registers in which information regarding insolvency proceedings can be published. In the Izoplac case had such registers been in operation at that time, commencement of the French proceedings and relief sought may have been avoided.

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