European Restructuring Update: France Introduces New Accelerated Safeguard Proceedings

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Summary

- France has now introduced a new restructuring tool following the enactment of Ordinance 2021-1193 (the "**Ordinance**"), which incorporates the Directive (EU) 2019/1023 on preventive restructuring frameworks (the "**Directive**") into local law.

- The Ordinance will apply to proceedings commenced from 1 October 2021 onward and primarily builds upon the current safeguard proceedings by introducing a new version of "accelerated safeguard" proceedings (the "**Accelerated Proceedings**"). However, in contrast to safeguard proceedings which are only available to solvent entities, the new Accelerated Proceeding will be available to both solvent entities and companies in financial distress.

- Restructuring plans implemented pursuant to the Accelerated Proceedings now include the mandatory use of creditor classes with the ability to impose a cross-class cram down (subject to the "absolute priority rule") in certain circumstances. Debtors also benefit from an automatic stay on creditor action from the point at which the proceedings are opened, subject to certain exceptions.

- Enhanced protections are also given to "new money" providers by way of limitations on such funds being subsequently restructured or clawed back, as well as preferred creditor status.

Why have these changes been introduced?

- The Directive requires member states in the EU to ensure that their local insolvency and restructuring laws include certain key features such as a debtor-in-possession proceeding and the ability to impose a cross-class cram down. One of the intended aims of the Directive is to ensure that companies in financial distress can access, at the earliest opportunity, restructuring tools which provide a higher probability of a company being rescued on a going concern basis.

- For some jurisdictions, such as the Netherlands, the Directive has required it to implement an entirely new restructuring process (having enacted the *Wet homologatie onderhands akkoord* (WHOA), which has radically changed the local Dutch restructuring regime. However, for jurisdictions such as France, which was already considered to be a very debtor-friendly jurisdiction to restructure, the changes to local law required to comply with the Directive are arguably more incremental as compared to other jurisdictions. Following its departure from the EU, the UK introduced the Corporate Insolvency & Governance Act 2020, which itself incorporates many of the key features set out in the Directive. Whilst the UK was no longer required to implement these changes following Brexit, the UK was heavily involved in the drafting of the Directive and prior to Brexit had already announced its intention to implement the Directive with a view to improving the UK's rescue culture.

How does it work?

- As part of a consensual workout process, a distressed debtor and its stakeholders have the option to first utilise “conciliation proceedings” (a pre-insolvency procedure overseen by a “conciliator” appointed by the court) to negotiate a restructuring arrangement within a four-month timeframe (capable of being extended for a further month). As any arrangement reached under a conciliation process does not bind dissenting creditors, debtors normally turn to safeguard proceedings if unanimous consent is not obtained during the conciliation process.

- During normal safeguard proceedings, the court mandates a six-month observation period for the debtor’s financial situation to be assessed and a rescue plan to be drafted and approved by its creditors. The Accelerated Proceedings fast-tracks this process by reducing the observation period to two months (although this may be extended for a further two months); it being specified that conciliation proceedings must precede the Accelerated Proceedings. However, the timeline for a restructuring is now reduced from a minimum of 10 months, to six months.

- In order for a distressed debtor, who is insolvent, to be eligible for the Accelerated Proceedings, it must be insolvent on a cash-flow basis for no more than 45 days as at the *conciliation* opening date.

Class composition

- In contrast to the required creditor committees in safeguard proceedings (which were not mandatory below a certain threshold and that will be replaced by creditors classes in the new proceeding), pursuant to the Accelerated Proceedings, creditors shall be divided into classes for the purpose of voting on any reorganisation plan.

- Unlike in the UK where the debtor proposes the constitution of classes for a scheme of arrangement or restructuring plan, in an Accelerated Proceeding, a court-appointed receiver will determine the constitution of classes based on there being a sufficient commonality of interest (and equal treatment) of creditors in the same class. Typically, secured and unsecured creditors will vote in separate classes, but additional classes of creditors can be created by the receiver. Like a UK scheme of arrangement or restructuring plan, only those stakeholders whose interests are affected by the proposed reorganisation plan are entitled to vote on it (i.e. impaired creditors or shareholders whose equity interests, or the rights attaching to their equity interests are being modified (e.g. by way of a debt for equity swap)).

- In order for a plan to be approved, two-thirds in value of each voting class must approve the plan (subject to the cross-class cram down). This contrasts with a 75% in value approval threshold for a UK scheme of arrangement or restructuring plan. As is the case with the UK restructuring plan (but not a scheme of arrangement), there is no additional numerosity requirement.

Cross-class cram down

- A new cross-class cram down ("**CCCD**") is available and can be utilised in Accelerated Proceedings if:

    a) the plan has been approved by a majority of the classes, provided that one of the classes consists of secured creditors or creditors senior to ordinary unsecured creditors, or

    b) failing that, at least one class of affected creditor has voted in favour of the plan, provided that such class is not a shareholder class, and is reasonably expected to receive a payment or otherwise retain an economic interest in the debtor following a liquidation, asset sale or another alternative arrangement.

- Furthermore, the court will also assess whether the plan places a dissenting class in a less favourable position compared to a liquidation, asset sale or other alternative arrangement (similar to the "no worse off" test in respect of UK restructuring plans).

- In the event of a dissenting class being a shareholder class, a CCCD in respect of that class will only be possible if the debtor has at least 150 employees and a turnover of at least €20 million. The dissenting shareholder class must also already be "out of the money" in a hypothetical liquidation scenario and the plan cannot include a full or partial transfer of the rights of that class. Where the restructuring plan provides for a capital increase by way of cash contribution or a set-off in respect of amounts due to the company, certain preferential rights are provided in favour existing equity.

Automatic stay

- Similar to normal safeguard proceedings, upon commencement of Accelerated Proceedings, there is an automatic stay on creditor action against the debtor. However, certain claims are excluded from this automatic stay, including claims arising from (a) debts incurred for the purposes of the proceeding being progressed, (b) debts incurred during the observation period, and (c) services provided to the debtor following the commencement of the proceeding.

- Separately, the opening of Accelerated Proceedings also prohibits counterparties from enforcing *ipso facto* clauses contained in contracts (i.e. termination rights following a failure by the debtor to pay a sum of money).

10-year term-out

- Under the Ordinance, the ability of the court to impose a 10-year term-out in respect of certain financial liabilities will not apply to Accelerated Proceedings. However, the 10-year term-out will continue to apply to normal safeguard proceedings, provided that creditor classes are not constituted as part of the proceedings.

The “absolute priority rule”

- The Accelerated Proceedings will adopt the “absolute priority rule” (which is optional for Member States under the Directive), meaning that if a CCCD is applied, dissenting creditors of a particular class must be repaid in full before a more junior class of creditor is repaid in full. However, the court may, at its discretion, make an exception to the rule if it is considered necessary to achieve the purpose of the plan and to the extent that it does not excessively affect the rights or interests of the impaired parties (e.g. if it makes commercial sense for unsecured trade creditors or equity to receive a distribution under the plan before a more senior class of creditor is paid in full).

- The application of the “absolute priority rule” in US Chapter 11 proceedings is controversial given that it is perceived to create hold-out value for dissenting creditors hoping to exact a better deal in any restructuring. It is for this reason that the “absolute priority rule” does not apply in the context of UK restructuring plans as the UK Government did not want ‘distressed vulture funds’ to have the ability to jeopardise what would otherwise be viable restructurings.

New money financing

- Another key feature introduced by the Ordinance is the protection of “new money” creditors. In the context of Accelerated Proceedings, cash contributions made to the debtor cannot be compromised in a subsequent restructuring and will receive preferred status in a liquidation scenario if such funds are made available to the debtor:

    a) during the observation period, subject to judicial approval (i.e. bridge-type financing to ensure business continuity during this period); or

    b) following the implementation of a restructuring plan (provided that the details of such financing is specified in the plan and approved as part of the wider plan vote).

- The amendments to the French restructuring framework as a result of the Ordinance can be viewed as a welcome change from both a debtor and creditor perspective, particularly in relation to the efficiency with which a restructuring plan can now be implemented as well as its automatic recognition within the EU. However, given that many of the reforms (such as class composition and cross-class cram downs) are generally untested in France, whether the Accelerated Proceedings becomes a credible alternative European restructuring tool remains to be seen.

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