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Proposals for the Reform of Insolvency Practice in France

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The Background to Reform

The French Government has been prompted to consider undertaking reforms to company law, insolvency law as well as the administration of the commercial courts. As far as corporate insolvency is concerned, the relatively recent adoption of new laws in 1984 and 1985,¹ which dealt with the framework for pre-insolvency measures and insolvency proceedings as well as the rules relating to insolvency practitioners,² has not made these laws immune to criticism and severe faultfinding, particularly from creditors' groups and financial institutions.³ These criticisms led to a further reform law in 1994 which tinkered with the procedural framework but left the law in relation to the professions largely untouched.⁴ Despite the 1994 reforms, further criticisms have emerged in relation to both insolvency practice and procedure, in particular from some very eminent members of the insolvency profession.⁵

It seemed, however, that reforms were not going to be attempted until the Government had sufficient material for a wholesale reform project. Matters became urgent when a scandal occurred during 1996-1997 which prompted close public scrutiny of the professions and intense press attention when it was alleged that two insolvency practitioners were involved in the disappearance of over FF 200 million from the coffers of companies they administered.⁶ During investigations, it was further alleged that a number of fellow insolvency practitioners were using their positions to further their own business interests. At the same time, the administration of justice in the commercial courts came in for much adverse comment, prompted by the

¹Law no. 84-148 of 1 March 1984 (Prevention of Business Difficulties Law), Law no. 85-98 of 25 January 1985 (Insolvency Law) and Law no. 85-99 of 25 January 1985 (Insolvency Practitioners Law).

²It should be noted that there are two separate professions in France, the administrator (*administrateur judiciaire*) and liquidator (*mandataire-liquidateur*) governed by the same Insolvency Practitioners Law. See Omar P, *Corporate Rescue Practitioners in France* [1996] 6 IL&P 188.

³For a history of movement towards reforms, see Omar P, *The Future of Corporate Rescue Legislation in France* (in two parts) [1997] 4 ICCLR 129 and 5 ICCLR 171.

⁴Law no. 94-475 of 10 June 1994 (Insolvency Reform Law). See Vallens J-L, *A propos de la reforme de la loi sur les entreprises en difficulte: Le rapport du groupe de travail du ministere de la justice*, (in three parts) *Les Petites Affiches*, 18, 21 and 23 February 1994, Nos. 21-23, at 11, 4, 15 respectively. There is an extensive bibliography in *Lamy Droit Commercial* at para. 2263 *passim*.

⁵See Soinne B., *Le Bateau Ivre (A propos de l'évolution récente du droit des procédures collectives)*, (in two parts) *Les Petites Affiches*, 14 and 16 May 1997, Nos. 58-59, at 2 and 4 respectively.

⁶This case, known as "l'affaire Sauvan-Gouilletquer" resulted in the arrest of both partners in February and April 1997 on charges of fraud, illegal acquisition of interests in companies and abetting criminal bankruptcy.

discovery made in a number of judicial districts that some commercial judges were involved in instances of potentially serious misconduct.⁷

Government Reaction

The overall level of public concern led Elisabeth Guigou, the Minister for Justice, to announce on 24 October 1997, during the General Conference of Commercial Courts in Paris, a raft of wide-ranging reforms which would centre around four key issues: the reinforcement of penalties for supervising judges who misuse their influence for personal ends, the closer scrutiny of insolvency practitioners' accounts and a requirement that funds generated by companies in insolvency be deposited with the official deposit-taker as well as a greater role for public prosecutors in insolvency proceedings. These reforms were also the subject of proposals presented to the Council of Ministers on 29 October 1997.

Following closely on these events, the National Assembly opened a parliamentary enquiry into the proposed topics of reform. The French Government's Inspectorate-General of Finances and Inspectorate-General of Judicial Services were also given a mandate to conduct an inspection into the areas of concern outlined by the Minister for Justice in her proposals. A recent press statement, issued by the Ministry of the Economy and Finances on 14 October 1998, reports the outcome of the enquiries.

The statement fleshes out a number of the proposals in light of the conclusions reached by the enquiries, although not all the recommendations made by the enquiries were accepted by the Government. In particular, a controversial reform proposal, suggested by Arnaud de Montebourg, the rapporteur for the Parliamentary Commission, to the effect that the profession of liquidator should be abolished, did not get a warm reception.⁸ In all, there are three principal areas that are the focus of attention in the statement, the reform of the commercial justice system, the reform of professions linked to commercial justice and the reform of the framework for insolvency law.⁹ This article will focus on those reforms affecting insolvency practice.

Reform of the Professions

The reforms in this section are aimed at curbing some of the excesses identified by the enquiries in relation to professions considered auxiliary to commercial justice. Indeed, the statement notes that where the enquiries found instances of excessive invoice amounts for professional services, rapid disciplinary proceedings have been instituted. The professions concerned are both types of insolvency practitioner, administrators and liquidators. Reforms

⁷A journalistic enquiry by Fortin D et al., published in *Challenges*, January 1998 edition at 48 passim highlights some of the causes of concern. The courts affected were said to include Paris, Bobigny and Nanterre (two courts just outside Paris) as well as Nice and St. Lô.

⁸See Vidal F, *Options Finances*, 6 July 1997, No. 507 at 6.

⁹These last reforms may also be prompted by the continuing unfavourable statistics. In 1993, 70,000 businesses became insolvent, with liquidation in 93% of cases resulting in the loss of 300,000 jobs. In 1997, fewer (58,000) insolvency proceedings were instituted but which affected more (325,000) jobs. 90% of these proceedings also led to liquidation.

relating to the two groups of insolvency practitioners in France centre around their status, adequate supervision of practice conditions and their remuneration by way of fees and other emoluments. Increasing access to the professions is also one of the topics under consideration.

I - Access and Transparency

Insolvency practitioners in France are considered to be auxiliaries of justice endowed with a court mandate enabling them to carry out their functions.¹⁰ The statement sets as a principle that other participants in insolvency proceedings should be able to gain all necessary information about the conduct of proceedings, thus supervising and, where necessary, challenging the methods by which insolvency practitioners exercise that mandate. The French Government considers that access to the professions needs to be opened up especially considering the relatively small numbers of professionals currently in practice as well as those deficiencies in practice recently brought to light.

The French Government is looking to the example of other jurisdictions, in which greater access to the practice of insolvency results in an admixture of professionals with a variety of useful skills. To this end, recruitment to the professions will be enhanced by reorganising training procedures and increasing the number and variety of placements available. In addition, quality will be maintained by requiring candidates to take an entrance examination prior to beginning training, unlike at present where the formal examinations occur at the end.¹¹ Nevertheless, the statement does provide that the two professions must be looked at separately, given that the functions of liquidators could, because of their technical nature, be more easily entrusted to other professionals, but that the primary task of the administrator, assisting or replacing company management during insolvency, involves a greater degree of skill.

As far as the profession of administrator is concerned, neither enquiry recommended that further measures allowing access to the profession were needed, as the current legislative framework already allows for access by other qualified professionals, including lawyers, notaries, bailiffs and court registrars.¹² In addition, the courts have the right to appoint as administrator in particular cases any person whether a member of the profession or not.¹³ This right is used very sparingly, although the view of the French Government is that, in future, it will recommend that judges use this option. A safeguard will be built in to allow the Public Prosecutor's office to supervise nominations, presumably so that valid objections to particular individuals will be brought to the court's attention speedily.

As far as liquidators are concerned, the emphasis is firmly on maintaining the nature of the court mandate but increasing access to the profession. The

¹⁰Art. 10, Insolvency Law.

¹¹Arts. 5 & 21, Insolvency Practitioners Law.

¹²Art. 13, Decree no. 85-1389 of 27 December 1985.

¹³Art. 2, Insolvency Practitioners Law.

French Government considers that courts should be able to choose from a greater number of professionals with a wider range of practice experience, provided that rules relating to ethical standards of behaviour and the avoidance of conflicts of interest can be maintained. Courts should also be able to nominate one or more persons to carry out tasks within the framework of liquidation, something which is very rarely done in smaller judicial districts because of the lack of availability of qualified individuals. In order to meet this, the existing framework, under which liquidators are organised within judicial districts under a Court of Appeal,¹⁴ will be amended to allow liquidators from across France to take on cases in any other district. According to the French Government, this will also help promote competition. Courts will, by analogy with the situation of administrators, be able to appoint other professionals or qualified personnel to conduct liquidation proceedings. This will be useful especially in smaller cases, where the services of a notary, bailiff or auctioneer may be more appropriate.

II - Fees and Supervision

Fees and charges have been the subject of the greatest number of criticisms,¹⁵ particularly given the almost arcane methods of calculation used to determine the level of fees.¹⁶ The reform of the fees structure is designed to ensure a correlation between the fees charged and the services rendered as part of the conduct of insolvency proceedings. This will also take into account proposals for reform of insolvency law and the resultant analysis of the real cost of each act and step incidental to proceedings and the profit margin for insolvency practitioners. As a first step, those fee levels most often objected to will be the subject of specific consideration. An example noted in the statement is the current practice of paying third parties to undertake certain tasks normally the province of administrators or liquidators. Fees for these third parties will in future fall to be paid by insolvency practitioners out of their own remuneration and will no longer be a charge on the assets of the insolvent company.

The French Government considers that, given the important sums often handled by insolvency practitioners and the potential for defalcation noted as a result of recent scandals, measures need to be introduced to control the management and disposal of funds collected during insolvency proceedings as well as to provide for effective supervision of their use. A draft decree, which has been submitted to the Council of State, contains a number of provisions designed to enhance the security of funds. These include an obligation to deposit all funds received during proceedings with the official deposit-taker and a requirement that insolvency practitioners declare any interest related to the case, the scope and definition of interest being defined more widely. In addition, professional norms and conventions will be introduced so as to harmonise the accounting standards of practitioners to enable transactions in all cases to be monitored on a day to day basis.

¹⁴Art. 20, Insolvency Practitioners Law.

¹⁵See Fortin D et al. Op. cit. at 57 and Vidal F, op. cit. at 7.

¹⁶Decree No. 85-1390 of 27 December 1985.

As far as supervision goes, the French Government will ensure that effective monitoring of practitioners' conduct will occur by the introduction of a two-tier system. At the lower level, this will permit practitioners themselves to institute checks on the basis of a national standard validated by the Ministry of Justice. A third party in the shape of an auditor will also be present to ensure a balanced view. At a higher level, regional inspectors attached to the Prosecutor's Office will be able to conduct inspections themselves or call in the investigation units set up by the Inspectorates-General of Finance and Judicial Services.

Reform Timetable

The statement notes that the reforms represent an important legislative task for Parliament and fixes a timetable for a rolling programme of reforms extending over five years. Measures which affect insolvency practice occur in the initial period of the programme:

Year	Legislation or Procedural Steps
1998	Legislation on supervision of insolvency practitioners
1999 (first semester)	Tabling of draft legislation containing: Reforms to the Insolvency Law and Prevention of Business Difficulties Law; Reforms to insolvency practitioners' fee structures.
1999 (second semester)	Legislation on insolvency practitioners' fees; Legislation on insolvency procedures.

Summary

Commentators have long criticised the insolvency professions in France for being susceptible to judicial and political influences. To this must now be added the temptation of gain. All the press statements made by the French Government, in particular the most recent release, have provided an insight into some of the compelling reasons the French Government has found to embark upon an extensive reform agenda within an ambitious timetable. The reforms address many of the criticisms of present insolvency law and practice, especially the need for transparency. Commentators will have the opportunity, once these reforms have been implemented, of determining the success of these proposals at curing lacunae and deficiencies in the law. In any event, most believe that these reforms are necessary in order to introduce a modern framework for enterprise in France and to maintain competition with the favourable legislative framework existing in other jurisdictions.

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