HammondsHausmann

La Revue

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Hammonds Hausmann Legal Newsletter

This is the first issue of our press review in English and is based on articles and clippings released in our French edition which is published monthly and aims to provide our readers with an update of legal issues and news from Hammonds' Paris office.

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The Revue n°1!
(Hammonds Hausmann legal Newsletter)

Dear all,

We are very proud to launch the first issue of "La Revue, Hammonds Hausmann's legal newsletter".

The French version of "La Revue" has circulated on a monthly basis for more than 10 years now.

The Revue's goal is to update foreign corporate clients on the main areas of French business law developments: namely Corporate, Company Law, Tax, Dispute Resolution and Arbitration, Competition, Employment, Construction and Real Estate, and Commercial and IP.

The approach is practical, to the point and user friendly.

Our aim is to help you to understand, focus and, hopefully, "digest" new regulations and case law on the above topics, but more importantly to link us to you.

For this new English version, which is intended to be issued on a quarterly basis, we have selected the most relevant recent articles and legal reviews from the French Revue.

It is well known that French business law is often perceived to be tricky, (which it is not), and difficult to understand for an Anglo-American lawyer or businessperson. We hope that La Revue will help you to understand it better.

Finally, it goes without saying that our team of lawyers are available and ready to assist you.

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Hammonds Hausmann was formed in 2001 by the merger of a highly international practice of French business lawyers practicing as Hausmann & Associés, with Hammonds, a leading commercial law firm , with its network of offices across the key European financial centres and in Beijing and Hong Kong.

This synergy allows Hammonds Hausmann to fully utilise the resources of a Global 100 law firm without compromise to the understanding of French business culture and the pragmatism and accessibility on which we are proud to have built our reputation in France.

Our objective is to form long-term partnerships with our clients. We value our approach of combining expert legal advice with strong business acumen and an in-depth understanding of our clients' business environment to offer commercial and flexible solutions, at acceptable cost and on time.

Our team in Paris brings together over 30 lawyers, ranging in origin, legal culture and language as diverse as Hammonds' offices across Europe and reflecting the truly international partnership that Hammonds offers its clients in their business dealings in France and abroad.

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Enjoy the Newsletter and do not hesitate to contact us or let us have your comments on the format or content of "The Revue". We would be delighted to publish any article or contribution from our readers, but also comments, news and criticisms.

I would like to take this opportunity to wish you all, a very happy and successful 2006!

A bientôt and we hope to hear from you soon.

Antoine Adeline

Office life

PORTRAIT

Christopher Wilde : an English man made in France

A graduate of King's College London and the Sorbonne, Christopher started his career as a solicitor in the Corporate and Commercial department of a City law firm in London. He was seconded to France for 18 months and is still here some 14 years later and was admitted to the Paris bar in 1996. He is the father of four children, two boys and two girls.

Christopher specialises in mergers and acquisitions and deals in cross-border transactions particularly in relation to Anglophone clients. He is equally at ease with French corporates as with Nasdaq or FTSE clients. He is involved in the communications sector and has particular experience in business process outsourcing.

In 1997 Christopher joined Hausmann & Associes as a partner accompanied by his assistant Isabelle Gabuteau. His English colleagues see Christopher as a product made in France and call him the "*Trick Frenchman*". In France, his slight British accent is barely noticeable and his perfect use of the French language is often noted.

Incorrect use of English is Christopher's *bete noire* and from time to time he sends emails entitled "*Ugly English to Avoid*" to educate his French colleagues on the subtleties of English and its differences with American-English.

Navigating two cultures is a pleasure for Christopher. He teaches English company law at Université Francois Rabelais in Tours. His home is also host to a Franco-English atmosphere with his (almost) bilingual family.

When asked about what he misses about life in England, he says "*the general unavailability of Marmite in France*", which from a French point of view, is not very serious. When asked if he doesn't feel a little French after all these years he says he prefers "*European*"!

HAMMONDS NEWS

Hammonds Hausmann gained 15 places in the top 100 law firms in France published by Décideurs and is one of the top 25 growing firms of the year.

Brussels Team Tops Tables for Fifth Year Running

The Brussels Trade team has been placed top of the list of law firms in the 'Customs, Trade, WTO and Anti-Dumping' section of the European Legal 500 directory, for the fifth year running.

Hammonds appears in the top tier along with Sidley Austin Brown & Wood, Van Bael & Bellis, Vermulst Waer & Verhaeghe, White & Case, and Wilmer Cutler Pickering Hale and Dorr.

The directory states that the office has 'grown to become one of Europe's leading trade law practices'. It also mentions Konstantinos Adamantopoulos, who heads the European Law team, and Edward Borovikov, who it refers to as a 'stalwart' and an 'expert in EU-Russia relations'.

Hammonds Germany

For the first time ever, Hammonds' German offices (Berlin + Munich) have been ranked by turnover in the top 40 law firms in Germany by Juve magazine.

Juve publishes the leading German legal magazine and annually produces the most important legal directory for the German market.

Hammonds was in good company with other international law firms including Clifford Chance, Freshfields and Norton Rose.

Peter Crossley Recognised at Legal Week Awards

Managing partner Peter Crossley was highly commended at the annual Legal Week Awards ceremony, held at Old Billingsgate Market in London on 30 November.

Peter came runner up in the Partner of the Year category, which was won by Nigel Knowles of DLA.

Finance Law Partner Makes TV Debut

Finance Law partner Laurence Winston recently made his television debut on CNBC's Power Lunch Europe show, presented by Daniel Mann.

The lunchtime show is a daily personal finance programme that assesses the first half of the trading day and offers expert opinion on investment strategies.

Laurence was invited to sit on a panel discussing corporate fraud and the likely collapse of Refco. Refco has been in trouble since its former chief executive was charged with fraud after concealing a $430 million loan ahead of a stock market floatation.

Laurence spoke about the effect that a collapse of Refco might have on the market, whether it was likely to lead to greater regulation, possible claims that may arise, and whether the company is likely to survive in its present form.

Avocats' favourites

- "Les Vignes de Marie "**, recommended by Baptiste Bellone**

  Two steps from the Arc de Triomphe, at the corner of the rue d'Artois and rue de Washington, there is a new wine cellar called "Les vignes de Marie". Upon entering you are warmly welcomed by Marie-Claude Orieux who has travelled the world to discover new wines (Californian, African, Hungarian) for you to sample. Of course, French wines are also available !

  Visit and discover new varietals and new tastes !

- Note the reopening of "**Le Petit Palais**" which is a "condensé" of the Louvres. Admission is free. Located in the heart of the business district it will only take you a couple hours to visit and bring home a good "picture" of French art.

- Next time you come to visit us in Avenue Velasquez, you must allow 40 minutes to visit our neighbour "***Musée Cernuschi***", the only French museum devoted exclusively to Chinese art. A jewel, just on the border of the *Parc Monceau.*

COMMERCIAL LAW

Breakdown in negotiations

(In the context of the purchase of a business)

The risks in French law

Antoine Adeline

By contrast to English law where the parties, other than in very limited circumstances, have the right to break off negotiations at any point and where there is usually no right to any indemnity, French law imposes a general obligation that the parties will negotiate in good faith.

LIABILITY FOR THE BREAKDOWN OF NEGOTIATIONS

If a party is "at fault" for the breakdown of discussions and if the other party can prove resulting loss, the party at fault may be liable to pay damages to the other.

In proving fault, the French Courts rely on the notion that the parties should conduct and, where relevant, terminate negotiations in "good faith".

In considering "good faith" the Courts will, in particular, refer to:

- The duration of negotiations and the stage at which negotiations were terminated
    - The breakdown in negotiations is more sensitive and must in particular be justified when there have been lengthy negotiations and when a binding agreement was very likely.
    - The Courts consider that a party is at fault if the negotiations have been prolonged artificially when it was clear to that party that the contract would not be concluded.
- The circumstances of the breakdown.
    - The suddenness of the breakdown and the existence of aggravating circumstances are considered by the Court to be exemplary of bad faith.

It is particularly important to note that an action for "*abusive breaking off of negotiations*" (*rupture abusive de pourparlers*) is an action in tort and may arise even where an appropriately worded letter of intent has been signed and even if this is subject to another law to that of France. Whilst of course this is not a reason to dispense with such a document, caution still needs to be exercised.

Under French law compensation for loss can include direct loss (e.g. costs linked to the negotiations, such as professional fees), indirect loss (such as loss of opportunity to contract) and possibly even intangible loss (e.g. loss of goodwill or loss of reputation).

SOME PRACTICAL ADVICE

1. **One must observe the principle of good faith in all negotiations**

   It is important to be able to demonstrate that in your dealings with the Sellers, you have been sincere, supplied correct information and been transparent and honest in negotiations.

2. **Avoid giving the impression that the agreement has been all but reached during the negotiations - (to the extent that this is commercially possible.)**

   This is particularly important when the approval of the board of the parent company needs to be obtained before signing. It is essential that the Sellers are reminded of this throughout the process and that if the final approval is either not obtained or conditional upon material changes being made to the then agreed terms, this must be communicated carefully. In such circumstances, we strongly suggest seeking legal advice prior to communication of such a change to the Sellers.

3. **Justify the breakdown of negotiations, giving explanations according to objective criteria (ie a change in market conditions)**

   It is vital not to continue negotiations when it is known that no contract will be reached.

However one should avoid hurried and sudden breaking off (a period of several days and maybe one or two weeks to allow for explanation and discussion is advised).

4. Precautions in relation to contractual documents amended by negotiations

- Include in successive drafts a reference to "*subject to contract*" or similar terminology.

  In comparison to English law, the French Courts place less value on this and it will be determined by the Courts according to the intention of the parties. Nonetheless, this is still an important precaution

- Retain at all stages outstanding conditions (and ensure the other party is informed of these regularly in writing, such as on the front page of successive drafts by way of note). These might include open due diligence items, approvals required (internal and regulatory), or terms of the deal itself. However, it may not be possible to rely on a condition too closely connected to the Buyer or dependent on its own will (such as internal approval or outcome of due diligence expressed as merely "*satisfactory to purchaser*") in avoiding a legal claim from the Sellers. An objective or independent condition will carry more weight.

Avoid however excessive reliance on stated conditions which could actually have been satisfied. In contrast to the English courts, French law looks much more at the spirit of behaviour than the letter of the document. For example, "*subject to due diligence*" may not be adequate if this could have been started a significant time beforehand. If due diligence is being delayed pending agreement, this should be made clear.

5. Record all exchanges which may justify termination in writing

It should be remembered that the French Courts place little value on evidence from witnesses.

Accordingly, great care should be taken as to the content of all relevant written correspondence, including e-mails.

Conclusion

The risk that an action will be brought for unnecessary or rash termination of negotiations can never be totally avoided. However, by taking a minimum of precautions, one can limit the risks considerably.

In practice, it is important to take legal advice as soon as possible and where necessary take the relevant steps to limit such risks.

Sudden breach of a contract – application to international contracts

Guillaume Taillandier

In a judgment of 14 October 2004, the Court of Appeal of Versailles gave an interesting application of article 442-6, I, 5 of the Commercial Code in relation to an international contract for the distribution of perfume.

Article 442-6, I, 5 of the Commercial Code states: "*The following acts committed by any producer, trader, manufacturer or person listed in the trade register render the perpetrator liable and entail the obligation to redress the prejudice caused: (...) Suddenly breaking off an established business relationship, even partially, without prior written notice* proportionate *with the duration of the business relationship and consistent with the minimum notice period determined by the multi-sector agreements in line with standard commercial practices.(...)*".

The contract, which was governed by French law, was concluded between a French supplier and a Colombian distributor for an initial period of three years. It was renewable and had a three-month notice period for termination. After sixteen years the French supplier decided to terminate the contract and gave three months notice as required by the contract.

The Colombian distributor objected that there was a "*sudden breach of a contract*" as set out in article 442-6, I, 5 of the Commercial Code and obtained compensation for not having received sufficient notice which the court said should have been at least one year.

The court's decision is not new. The court stated that complying with the terms of a contract may not be enough to comply with the provisions set out in article 442-6, I, 5 of the Commercial Code.

By handing down this decision, the court effectively extended the principle set out in article 442-6, I, 5 of the Commercial Code to protect a foreign distributor. The question is whether the court states that the liability is contractual or tortious. Although we do not know for sure, the court seemed to imply that the damage was suffered in France and that it was therefore appropriate to apply French law.

COMPETITION

DGCCRF's Guidelines on the regulation of mergers are now on line

Guillaume Taillandier

The wait is over. Well, almost. It was beginning to seem that the project to issue guidelines on the control of concentrations (the "Guidelines"), which had been announced on 13 December 2002, would remain just a proposal. The Guidelines were finally published on the DGCCRF's website last July. Although the DGCCRF (the French Competition Authority) acknowledged that a delay of two and a half years was inexcusable, it hoped to be able to explain and present the content of these Guidelines.

Following the example of the guidelines published by the European Commission and by competition authorities in the EU Member States, the Guidelines provide above all else an insight into the manner in which the DGCCRF intends to assess a merger or acquisition coming under its remit. These Guidelines present the procedure (for notification and clearance) and reiterate the requirements upon the DGCCRF to determine the risk of the creation, or strengthening, of a dominant market position and the prevention of the distortion of competition upon the market.

The Guidelines are formidable: 162 pages in all! However, the DGCCRF has thankfully inserted at the beginning of the document a succinct 16 pages summary to the Guidelines. The relevant French legislation has also been attached as an annex.

This said, the DGCCRF has deliberately taken an academic role preferring a long document with concrete examples and analysis of decisions to that of a short and dense text (as preferred by our American cousins or certain factions of the European Commission).

In a recent presentation for the journal, "Competition", the deputy head of the DGCCRF, Madame Caroline Montalcino, stated that two important events took place from the original announcement in December 2002 which caused the delay in publication of the Guidelines: First, far more decisions have been taken by the DGCCRF than had previously been the case (600 decisions; 300 of which were in 2002). Although the relaxing of the individual threshold has led to a reduction in notifications, there are still on average 150 notifications to the DGCCRF per annum. These decisions have had to be made without an increase in budget. Many of the problems faced in these decisions are replicated in the Guidelines. Second, the adoption of the new Merger Regulation by the European Commission (Regulation 139/2004) resulted in a change to the manner in which the European Commission and the Member States are bestowed jurisdiction to assess a merger or acquisition (and may refer issues amongst themselves). The Guidelines provide numerous references to issues referred to the DGCCRF by other EU competition authorities.

A regret: the Guidelines are sadly lacking in real information on the conditions under which a merger or acquisition can be reversed (i.e. de-merger) on the basis of Article L.430-9 of the Commercial Code which outlines the possibility for the Competition Council to ask the Minister to order the dismantling of a merger or acquisition that contributes to an abuse of a dominant market position.

That said, the Guidelines are to be commended for the useful information provided in the annexes to the Guidelines, most notably on: the treatment of capital investment transactions (Annex 1); questions relative to distribution contracts (Annex 2); agricultural co-operatives (Annex 3); and questions relevant to enterprises in difficulty (Annex 4).

So the delay in publishing the Guidelines has arisen, ironically, from the constant changes and evolution of competition conditions on the market.

EMPLOYMENT

The "*nouvelle embauche*" contract

Elisa Bernad

Order N 2005-893 of 2 August 2005

The media has greeted the arrival of this "new product" with scepticism – commenting that the work market place is already saturated with a number of different types of contracts of whose names, more than the content, change according to the government's wishes.

However, it must be admitted that the "*nouvelle embauche*" contract is different from other contracts. Although it is only intended for businesses with 20 or less employees, it nevertheless concerns all contracts of indeterminate length in so far as the contract contains a trial period of 2 years which can be broken by the employer at any time (subject to respecting a notice period of 15 or 30 days) and without having to give any reason.

The employer does not have complete freedom to dismiss employees at will. The fact that the contract can be broken at any time does not exonerate the employer from respecting the rights of his employees. Similarly, a protected employee's contract cannot be terminated without prior authorisation of the labor inspection.

The "*nouvelle embauche*" contract does not eliminate the risk of litigation where the employer terminates the contract without cause. It is anticipated that employees and even judges will pay more attention to whether or not the termination is founded or motivated by reasons related to an employee's private life, political opinions or is discriminating (for example on grounds of religious beliefs or sexual orientation).

This order is not a blank cheque for companies. Any termination of an employment contract that is not founded on professional inadequacy, disciplinary or economic grounds could incite employees to seek justice from the employment tribunals.

The fact that there does not have to be a reason for terminating the employment contract does not mean that there is no risk of litigation from employees. It is the employer's responsibility to ensure that they effectively manage the employment contract. An employee whose contract has been terminated after nearly two years of service will benefit from the required 30 days notice period but it is advisable in any case to ensure that there is some provision in the contract relating to the end of the long trial period. Particular attention should be paid to employees on the "*nouvelle embauche*" contract and employers should ensure that periodic evaluations are in place between the employer and employee so that both parties are fully aware of the implications of the contract.

It may be that the "*nouvelle embauche*" contract is part of the response to unemployment but it will not allow companies to dispense with regularly training and evaluation of their employees. Employers who are not mindful of the implications of the new legislation could be caught out and indeed the first claim began one month after the introduction of the contract.

CIVIL PROCEDURE

French class action

Agnès Bérenger

Jacques Chirac's desire to implement a system of court class action to enable consumers to combat the abusive practices of certain industries should have been finalised by the beginning of this year by a draft law, but it was delayed.

The parties involved in the draft - consumer associations and lawyers - point out that the procedure will give small complainants the ability to be heard in the context of a unified complaint.

While a class action procedure already exists in France, the *"joined action"* it is not widely used because of its complexity. It involves collecting all the claims of the complainants which is a difficult task to manage.

Up until now companies engaging in abusive practices did not have much to fear from the French legal system but the situation could change with the draft law.

Critics of the law, namely the Medef, say that class action is an American menace and that more often than not the proceedings benefit the lawyers and not the complainants.

It could be that the ethical code for lawyers in France, which states that lawyers may not be remunerated exclusively on the result of a case, would prevent lawyers from unfairly profiting from class action lawsuits.

A working group of the national bar council wrote a report to the minister of justice which was favourable to the introduction of a new form of class action lawsuit. The report pointed out that for the new kind of lawsuit to be successful the lawyers' ethical code must be flexible on two points: the prohibition on soliciting business and remuneration of lawyers.

However, a working group consisting of Medef representatives, consumer associations and lawyers was not in favour of introducing the procedure. In a report given to government ministers and published on 19 December, the group proposed three alternatives:

- a simple adjustment to the joined action;
- a collective action similar to an American class action suit where the collective action would be lodged by a group of consumers constituted of people who expressly wish to be included in the action or a collective action including all consumers except those who expressly wish to be excluded;
- an action led by an association following which the consumers could act individually to obtain compensation.

A new consultation is being launched and will continue until 1 March. After this date the government must deposit the draft law.

INSOLVENCY

Appointment of English administrators not contrary to French public policy

Antoine Adeline

In May 2005, we reported that the appointment of administrators by the English High Court in respect of SAS Rover France was held by the French Commercial Court to be a valid appointment pursuant to the EC Regulation Insolvency Proceedings (1346/2000) ("*Regulation*").

Notwithstanding the very robust and commercially grounded decision of the Commercial Court of Nanterre, the appointment of the English administrators in respect of SAS Rover France has been the subject of an appeal by the French Attorney General who pleaded several articles under the Regulation. The decision of the French court of appeal has been handed down on 15 december; it is another success for Hammonds Hausmann and a further endorsement of the application of the Regulation by the court of appeal in France.

The Appeal

The Attorney General brought his appeal against the application of the English administration order on three main grounds:

The English administration order that determined that the centre of main interests of SAS Rover France to be in England was invalid.

The application of English insolvency procedure, in particular with regard to the rights of the French employees, was contrary to French public policy.

There should be a secondary insolvency procedure opened in France in respect of SAS Rover France.

Validity of the jurisdiction of a Member State

It was argued by the Attorney General that the French courts have a duty to verify the jurisdiction of the court of another member state, not only to determine that the correct criteria for choosing the jurisdiction has been applied, but also to ensure that the centre of main interest was correctly determined to be within the jurisdiction.

Such an argument, if sustainable, would be entirely contrary to both the spirit and the terms of the Regulation. The aim of the Regulation is to improve the efficiency and effectiveness of insolvency proceedings with a cross border effect. Automatic recognition of another state's insolvency proceedings is a central principle of the Regulation. To require the courts in each Member State to verify insolvency proceedings opened in another Member State would be a barrier to such efficiency. For this reason, Article 17 of the Regulation provides that the opening of main proceedings in a Member State shall, "*with no further formalities*", produce the same effects in any other Member State as under the law of the country in which the proceedings are opened.

The French appeal judge held that the only obligation on the French courts is to ensure that the decision to open main proceedings in another Member State has complied with the conditions necessary for the proceedings to be recognised in France. If those conditions are met, namely that the court has jurisdiction under Article 3 of the Regulation because the company's centre of main interest is located within that Member State, no further formality or verification is required.

When can main proceedings commenced in another Member State be refused as contrary to French public interest?

The issue of appointment of administrators from outside France in respect of French incorporated subsidiaries of international groups is not new. The equally controversial appointment of English administrators of the French subsidiary of the ISA Daisytek Group of Companies continues to be the subject of legal argument in France: the decision on the second appeal by the Public Prosecutor is expected in January/ February 2006. However at Court of Appeal level, there has now been a second decision recognising that the Regulation makes this possible.

Article 26 provides that a Member State can refuse to recognise insolvency proceedings opened in another Member State when they would be manifestly contrary to its public policy. The Regulation describes this as meaning contrary to its fundamental principles or the constitutional rights and liberties of the individual. The Attorney General relied on this article to say that the English insolvency procedure ignored the French employee's rights.

The French court of appeal took the view that the grounds for non-recognition should be reduced to a minimum. In this particular case, Hammonds Hausmann and the administrators had taken significant steps to consult with local insolvency practitioners to ensure full compliance with French employment law, had complied with all the duties of notification and consultation and had made financial provision to meet the claims of the French employees on terms equivalent to French law. The English administration was therefore found not to be contrary to French public policy.

Opening secondary proceedings

Not a point of appeal but as a separate action, the Attorney General requested that secondary proceedings be opened in France. This was rejected by the Court of Appeal; the Attorney General was unable to demonstrate that there would be any advantage, in particular the protection of local interest or a better realisation of assets, in the commencement of secondary liquidation proceedings in respect of SAS Rover France. It was satisfactorily demonstrated, on behalf of the English administrators, that the administration had been successfully run, as account had been taken of all relevant interests, and the likely outcome was that the sale operations would be continued for some time. Secondary proceedings would only add unnecessary costs and formalities, to the detriment of the creditors.

What next?

The interpretation and application of the Regulation continues to be a fast growing area of law. Currently pending is the European Court of Justice's decision in the Eurofoods/ Parmalat case, which includes arguments on public policy between Ireland and Italy. This is likely to be succeeded by the further French decision in ISA Daisytek.

This French court of appeal decision in SAS Rover France has established some principles.

New French insolvency law enters into force on 01/01/2006

Antoine Adeline

Inspired by the American bankruptcy law known as "*Chapter 11*", the "law to safeguard businesses" is aimed at helping businesses to avoid financial difficulties and to allow companies in bankruptcy to avoid liquidation.

The law of 1985

According to statistics, the law of 1985 did not have the desired results – more than 50,000 businesses disappear every year.

The fact that the legislation of 25 January 1985, updated in 1994, lacked efficiency and was revealed to be incongruous with the actual economic context (globalisation, deindustrialisation, RTT) can also be attributed to the shortcomings of company directors.

Reform

The objective of the new text is to encourage research into the handling of the difficulties of companies. A declaration of suspension of payments is not an automatic indication that a company will be subject to the opening of a collective procedure.

The law of 1985 set out a wide variety of procedures which at times made the situation unnecessarily complex.

In the search for a solution that would allow the company to continue operating, the law considers that "*the debtor is better placed to appreciate which procedure is better adapted to the situation*". During a set period, the director has the following choices: the ad hoc mandate, reconciliation, or the legal route.

Friendly procedures

The principle aim of friendly procedures is to facilitate negotiation between companies in financial difficulties and their creditors. The advantages of such an approach are as follows:

- anticipation – the principle cause of failure is when a procedure is opened too late
- confidentiality – since security of agreements is one of the reform's objectives

The ad hoc mandate

The ad hoc mandate is aimed at "*finding a solution when a company proves that its financial difficulties are compromising its ability to continue operating*".

This procedure is started by the chairman of the Commerce Court at the request of the head of the company.

The fact that an ad hoc mandate is flexible, confidential and does not have strict opening conditions makes it a preferred "*friendly procedure*" for companies in financial difficulties.

"Reconciliation"

The success of this procedure depends on the contractual nature and confidentiality of its application.

In replacing the old "*friendly regime*", reconciliation can be requested "*when companies run into financial, legal or economic difficulties whether known or foreseeable*".

During an observation period a company and its creditors will strive to reach a reconciliation agreement. If this is successful then the reconciliation agreement will be certified by the chairman of the Commerce Court. For a greater degree of security it could be recognised by the Court itself if three conditions are met:

- the company has not suspended payments for more than 45 days;
- the agreement aims to guarantee that the company will continue operating; and
- the agreement does not affect the interest of creditors who are not party to it.

The benefits of the agreement are important:

The agreement approved by the Court makes it difficult to challenge resolutions that were passed when the company was suspending payments at the time of the reconciliation, except in the case of fraud or abusive conduct.

The opening of a reconciliation procedure suspends all requests for the opening of a bankruptcy or liquidation procedure.

The head of the company does not lose control of the company.

Another advantage similar to that provided by Chapter 11, relates to creditors who bring funds to the company. They will be reimbursed in certain circumstances after employees and legal costs have been paid.

Legal procedures

When a friendly procedure is ineffective, the company in financial difficulties must ask for a bankruptcy or liquidation procedure to be opened within an eight day time frame starting from the notification of the end of the reconciliation procedure, or the final decision by the court to recognise the agreement.

The safeguard procedure

The safeguard procedure is an important part of the reform of the law in this area. It is put into place at the request of the director when a company is experiencing known or expected financial difficulties that are likely to lead to bankruptcy.

This procedure is actually an intermediary step between a friendly procedure and bankruptcy.

The safeguard procedure provides for the opening of a two month observation period with the aim of reaching a safeguard plan negotiated with the creditors. To this end, it also provides for two committees of creditors – one committee for the establishment of credit and a committee of principal suppliers.

The idea is that creditors are well placed to understand the urgency and complexity of the company's situation and have a vested interest in making the procedure work.

The creditors who are due to be paid in the observation period must still be paid. If it seems that after the opening of the safeguard procedure that the debtor was already suspending payments at the time of the opening then the court takes note of this date.

A company that requested the safeguard procedure, but who does not suspend payments, may be put into liquidation if their financial state is brought to light during the course of opening the procedure.

On the other hand, if the company is suspending payments at the time of the opening of the safeguard procedure, then this can be converted into a bankruptcy proceeding.

Bankruptcy

The new law does not fundamentally change the bankruptcy procedure.

The head of a company must request the opening of a bankruptcy procedure within 45 days of officially suspending payments and if not then within this same timeframe request the opening of a reconciliation procedure.

A bankruptcy procedure can also be opened at the time of the incident that started the observation part of the safeguard period (if the company is unable to finance the observation period or when the continuation plan is not accepted by the creditor committees).

The administrator can help the debtor or can help manage the company.

Under the new law creditors with a surety will have enhanced rights.

Liquidation

Liquidation, which terminates the operations of a company or realises the capital of the company, is only for companies who have suspended payments and are completely unable to carry on activities even with a bankruptcy plan.

Liquidation is proceeded with directly. There is no need for the formality of opening a procedure of safeguard or a bankruptcy procedure.

If the total or partial liquidation of a company is planned, or if it is in the interest of the creditors, then the company may carry on its activities.

Alongside the procedure provided for by the general law, a simplified liquidation procedure could be available to SMEs.

This simplified liquidation procedure is possible if the following conditions are satisfied:

- if the company's activities do not involve immovable goods
- if in the six months prior to the opening of the procedure the number of employees and the turnover not including tax is less than the threshold set out in the decree.

Sanctions

The law reduces and simplifies the sanctions regime by doing away with secondary causes at the end of sanctions and rendering incompatible the liability for insufficient assets with a safeguard or bankruptcy plan.

The text limits the liability of banks for negligently providing support to the following circumstances: fraud, involvement in the management of the company, taking inappropriate guarantees.

Conclusion

The new procedure seems to be a good move forward and any complexities are bound to be ironed out in case law and jurisprudence.

DATA PROTECTION

Frédéric Saffroy

Is France against Whistleblowing ?

In the ongoing love-hate relationship between France and the US, France is once again at the forefront of the *Résistance* against the effect of US legislation on European domestic legislation and social and cultural behaviour. The latest controversy concerns whistleblowing procedures which must be implemented in all companies listed on a US stock exchange as a result of the *Sarbanes-Oxley Act* of 2002.

In May 2005, the French Data Protection Agency ("**CNIL**") refused to approve two whistleblowing procedures set up by US companies. These decisions were unsurprising given France's historical reluctance to implement a legal framework for this practice. The cultural background to this position is the occupation of France during the Second World War and an ongoing sensitivity to any form of denunciation. There are also reservations about whistleblowing in other EU countries due to recent or historical experience of informers in totalitarian or autocratic states. The CNIL's decisions, confirmed by a French Court decision in September 2005, came in the middle of a public debate on the implementation of a corporate Code of Ethics that some unions consider to be illegal.

However, a more flexible position was adopted in November 2005 when the CNIL released a set of guidelines that will (i) form the basis of its rules which will be published in January 2006; and (ii) form the basis on which the Article 29 Data Protection Working Party is expected to adopt a pan-European position on whistleblowing.

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The implementation of whistleblowing procedures in France raises issues in three areas of French law:

(i) General criminal law (see **§ 1.**)

(ii) Labour law (see **§ 2.**); and

(iii) Data Protection law (see **§ 3.**).

GENERAL CRIMINAL LAW

1.1 General provisions of the French criminal law concerning denunciation

In France there is no general obligation of denunciation except in relation to crime. Importantly, this kind of denunciation can only be made to the public prosecutor or to the police and failure to report a crime could lead to criminal prosecution (section 223-6 of the *Code penal* – Criminal Code).

There are certain individuals and organisations that are legally obligated to inform the public prosecutor of any violation of law which constitutes a misdemeanour ("*delit*") under French

criminal law. Chartered accountants and statutory auditors as well as attorneys and bailiffs amongst others, have a specific duty to report to the *Ministre du commerce* any sum or transaction suspected of being related to illegal drug trafficking, terrorist activities, corruption or any other organised criminal activity (section L. 562-2 of the *Code Monétaire et Financier* – Monetary and Financial Code). Any other legal entity or individual whose professional activities involve dealing, managing or controlling investments is obliged to report to the public prosecutor any financial transaction he knows or suspects to originate from any illegal source (section L. 562-1 of the *Code Monétaire et Financier*).

Subject to the above, French law dictates that employees cannot be mandated by their employer to blow the whistle.

1.2 Defamatory denunciation

The dangers of whistleblowing procedures include:

(i) a whistleblower uses the procedure to maliciously denounce a colleague with false information;

(ii) the whistleblower provides facts which are unproven and/or unsupported by sufficient evidence.

Article L. 226-10 of the *Code Pénal* provides:

> *"A denunciation made by any means and directed against a specific individual, of a fact that is liable to cause judicial, administrative or disciplinary sanctions and that the maker knows to be totally or partially false, where it is sent either to a judicial officer or to a judicial or administrative police officer, or to an authority with power to follow it up or to refer it to the competent authority, or to superiors or to the employer of the person concerned, is punishable by five years' imprisonment and a fine of € 45,000."*

In view of the above, if a company implements a whisteblowing procedure it could conceivably be deemed an accomplice to the whistleblower under section L. 121-7 of the *Code Pénal* and thus subject to the same penalties as the errant whistleblower.

LABOR LAW

2.1 Monitoring and control of employees

Section L. 120-2 of the *Code du travail* (Labour Code) prohibits employers from restricting individuals' rights unless justified by the employees' duties or proportionate to the employer's purpose. The employer is nevertheless entitled to monitor and process sound and data in relation to employees. However, under the provisions of this article, the data must be adequate, relevant and not in excess of the purpose for which it is processed.

2.2 Informing and consulting the Works Council

The reasons for obtaining the data must be clear and legitimate, and surveillance and monitoring systems must be implemented prior to data collection. Section L. 432-2 of the *Code du travail* states that the Works Council must be informed and consulted prior to the implementation of any significant project with regard to new technologies which could impact upon employees' employment, qualification, remuneration, training or labour conditions. Information in relation to such a project must be communicated to the Works Council one month prior to the meeting on the proposed technology.

The *Code du travail* states that the Works Council must be consulted prior to the automatic processing of data and/or modification to the processing systems (section L. 432-2-1 of the *Code du travail*). This obligation is also applicable if any method or system is implemented which allows for employees to be monitored. Non-compliance with these provisions constitutes a criminal offence of impediment to the Works Council missions (called "*délit d'entrave*") for which an employer could be liable to one year's imprisonment and a fine of 3,750 euros (section L. 483-1 of the *Code du travail*).

NB : It should be noted that in relation to a similar German provision [1] a German Labour Court [2] ruled on 15 June 2005 that a *Wal-Mart* whistleblowing hotline was illegal because it was

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[1] Section 87 - Right of Co-Determination under the *German Works Council Constitution Act (Betriebsverfassungsgesetz – BetrVG).*

[2] The 5th Division of the Wuppertal Labour Court (*Arbeitsgericht*) on 15 June 2005.

implemented without first consulting the Works Council. In relation to the telephone hotline, the Court stated that :

(i) the company's Code of Ethics contained a whistleblowing procedure and threatened disciplinary action in case of breach and therefore required Works Council consent; and

(ii) the telephone hotline constituted technical equipment designated to monitor employee conduct which also required prior consent from the Works Council.

2.3 Amendment to the *Règlement Intérieur*

The *Règlement intérieur* (Internal Regulations Handbook) sets out an employer's disciplinary rules and potential sanctions for non-compliance (section L. 122-34 of the *Code du travail*). From a French labour law perspective whistleblowing may have consequences for the denounced individual if the information is correct, but also for the whistleblower if the information turns out to be inaccurate. Both actions can be penalised under the *Règlement intérieur*. It is therefore necessary, if a whistleblowing procedure is implemented, to amend the *Règlement intérieur*.

Under French labour law the *Règlement intérieur* cannot be implemented or amended unless it complies with the following:

- it must first be submitted to the Works Council, or if a corporation does not have a Works Council to the employees' representatives;
- it must be submitted to the Health & Safety Committee for approval on matters related to its competence (*see* ***German case above***);
- it must be communicated to the Labour Inspection; and
- it must be notified to the *secretariat-greffe* of the *Conseil des prud'hommes* (Labour Court).

2.4 Protection in France of employees who report certain offences

Employees are entitled to report the following misdemeanor offences: discrimination, harassment and sexual harassment. The *Code du travail* states that employees cannot be sanctioned for "*testifying*" or "*reporting*" facts in relation to these offences. Such a report can be made to any trade union of the company that is then allowed to sue the alleged defendant (section L. 122-45 and *seq*. of the *Code du travail*).

2.5 The 15 September 2005 decision of the *Tribunal de grande instance* of *Libourne*

On 7 July 2005, a case was brought before the *Tribunal de grande instance* (First Instance Civil Court) in *Libourne* (*Gironde*) for summary proceedings (fast track, known in France as "*référé*") by the local branch of a national Trade Union (the "*CGT*") and the Works Council against the French subsidiary of BSN Glasspack. The Works Council had been informed about the process and the dedicated tools and were not satisfied with company's answers and the risk of anonymous denunciations.

The Court order ("*ordonnance*") was issued on 15 September 2005 [3] and stated that regardless of the ultimate treatment of information received on a hotline, there was a risk of employees being anonymously denounced, having an internal investigation launched against them and being the subject of sanctions without ever having been given the right to defend themselves. Moreover, the Court said that the present system (*i.e.* the hotline), like the one that was planned for BSN Glasspack's factory in France, with the concomitant risks of slanderous denunciation, seemed disproportionate to the objectives of the US law.

The Court also said that the mere possibility of damage to an employee, who could be a victim of anonymous denunciation made by the means of a private and uncontrolled system that cannot be justified by the interests of the company, is sufficient to impose interim measures. As a protective measure, the judges ordered the Company to remove controversial notices from the notice boards until a full ruling is issued. Interestingly, the Court indicated that an agreement with employee representatives in relation to the methods of enforcing US legal requirements would be acceptable if it also complied with French law.

[3] Tribunal de grande instance de Libourne, 15 septembre 2005, "*Comité d'établissement BSN Glasspack, syndicat CGT du personnel de BSN Glasspack c/ SAS BSN Glasspack*", Dossier n° 05-00143.

DATA PROTECTION IN FRANCE AND THE DECISIONS FROM THE CNIL

3.1 The CNIL's decisions dated 26 May 2005 (*Mc Donalds* & *CEAC*)

On 16 June 2005, the *CNIL* published two decisions of 26 May 2005 in which it refused to authorise the processing of personal data obtained by means of whistleblowing systems through which employees could report wrongdoing or misconduct on the part of their colleagues.

The systems in question were to be implemented by the French subsidiaries of American companies in accordance with the Sarbanes-Oxley Act of 2002. The requests for authorisation concerned systems which permitted employees to disclose any practice or behaviour of other employees which might be in breach of binding corporate rules or the company's code of ethics to the managers of the subsidiary or parent company by telephone, email, fax or post.

In its decisions, the CNIL made the following points:

a. The systems in question were disproportionate with regard to

(i) the purpose of the personal data processing; and

(ii) the risk of false accusations.

b. The employees that are the subject of a disclosure are neither informed of the allegations that bring their professional integrity into question at the time the disclosure is made nor do they have the ability to object to the processing of their personal data. The method of collecting and processing this data could therefore be regarded as unfair.

c. The ability to implement this 'ethical alert' on an anonymous basis would only increase the likelihood of false accusations.

It should be noted that the CNIL refused the request for authorisation from *McDonald's France* even though:

- the transfer of data to the USA was to be governed by a framework agreement on the transfer of data; and
- the use of the "*alert system*" was optional.

The CNIL also refused an authorisation request from *Compagnie Européenne d'Accumulateurs* (CEAC) (a subsidiary of *Exide Technologies*) despite the fact that disclosures would have been made to an American service provider acting on behalf of the parent company and that, as the calls were going to be made in French, a second American service provider would also have intervened.

The CNIL's decisions prohibited the implementation in France of any system, process, procedure or policy through which employees denounce the behaviour of their colleagues and involving the processing of personal data.

Furthermore, any provision in an employment contract obliging the employee to report to senior management any wrongdoing is also likely to be unenforceable, if not unlawful, under French law unless the employee is subject to a specific statutory obligation to report misconduct by virtue of his or her senior status (*see **§ 1.1** above*).

3.2 The CNIL's Guidelines for the implementation of whistleblowing schemes

(10 November 2005)

Following its refusal to authorise the whistleblowing procedures described above, the CNIL launched a consultation on the matter with the SEC, the French Ministry of Labor and others concerned about whistleblowing procedures (businesses, lawyers, trade unions, etc.). The result of the consultation was a set of guidelines published by the CNIL on 15 November 2005.

The following principles form the basis on which the CNIL will approve or refuse a whistleblowing scheme :

The whistleblowing scheme must be **based either on a French legal requirement** [4] or on the **legitimate interest of the company** [5] - such as the obligation to comply with a foreign legal requirement. The CNIL considers that the **Sarbanes-Oxley Act** falls within the latter category.

Only whistleblowing schemes relating to the following **four areas** will be automatically acceptable:

- banking;
- accounting;
- finance; and
- the fight against corruption.

Whistleblowing schemes relating to anything else will be considered on a case-by-case basis.

The use of the whistleblowing systems **should not be optional.**

Only certain categories of employees can be involved in a whistleblowing scheme, *i.e.* employees involved in banking, accounting, finance or corruption.

The CNIL does not prohibit anonymous whistleblowing but states that anonymous reports should be subject to specific precautions.

Information on the whistleblowing procedure must be clear and extensive.

One or more individuals must be responsible for the scheme. If the whisteblowing scheme is **administered by an external entity**, then the CNIL states that the contract for services should contain: **(i)** a strict duty of confidentiality; **(ii)** measures to avoid the data being used for other reasons; **(iii)** a limited data retention period.

In relation to the retention of data, the CNIL states the following:

- any data relating to a report which is found to be unsubstantiated must be **deleted immediately** ;
- data that required verification should **not be kept for more than two months** after the verification work is finished ;
- as soon as a report leads to disciplinary action or a court proceeding, the data may be retained for as long as necessary.

Data collected in a whistleblowing scheme **can be communicated to another company or organisation within the group of companies** only if this is necessary because of the nature of the whistleblowing scheme or the nature of the data collected. Data transferred outside the European Union must comply with relevant international data transfer regulations.

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These are the principles that the CNIL has outlined for the implementation of a whistleblowing procedure. It should be noted that these guidelines do not consider employment law or other applicable legislation.

It is therefore important to note the following :

To the extent that the whistleblowing scheme affects employees' duties (work contract, collective labour agreement, internal rules etc.) there must be preliminary consultation and information sessions with the relevant employee representatives.

If information collected from a whistleblowing scheme in France is required for a foreign legal proceeding (whether or not in the EU) then it must be transferred to the relevant authority in the jurisdiction in compliance with international conventions (*i.e.* the Haye Convention of 1970). If these procedures are not complied with then the person or persons who transmitted the information could be liable under the law of 26 July 1968 (blocking statute) to 6 months imprisonment and a fine of 18,000 euros.

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[4] Art. 7, 1°, of the Act n° 78-17 of 6 January 1978 on data processing, data files and individual liberties (as amended by the Act of 6 August 2004) (the "**Act**").

[5] Article 7, 5°, of the Act.