# How to restructure your creative business in France | Restructuring & insolvency law firm Crefovi

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## Almost any medium-sized and large creative business has overseas operations, in order to maximise distribution opportunities and take advantage of economies of scale. This is especially true for fashion & luxury businesses, which need strategically-located brick & mortar retail outlets to thrive. However, such overseas boutiques may need to be restructured, from time to time, in view of their annual turnover results, compared to their fixed costs. What to do, then, when you want to either reduce, or even close down, your operations set up in France? How to proceed, in the

# most time and cost efficient manner, to restructure your creative business in France?

One thing that needs to be clear from the outset is that you must follow French rules, when you proceed onto scaling back or even winding up your operations set up in France.

Indeed, in case you have incorporated a French limited liability company for your business operations in France, which is a wholly-owned subsidiary of your foreign parent-company, there is a risk that the financial liability of the French subsidiary be passed onto the foreign parent-company. This is because the corporate veil is very thin in France. Unlike in the UK or the US for example, it is very common, for French judges who are assessing each matter on its merits, to decide that a director and/or shareholder of a French limited liability company should become jointly liable for the loss suffered by a third party. The judge only has to declare that all the following conditions are cumulatively met, in order to pierce the corporate veil and hold its directors and/or shareholders liable for the wrongful acts they have committed:

- the loss has been caused by the wrongful act of a director or a shareholder;
- the wrongful act is intentional;
- the wrongful act is gross misconduct and
- the wrongful act is not intrinsically linked to the performance of the duties of a director or is incompatible with the normal exercise of the prerogatives attached to the status of the shareholder.

The specific action of liability for shortfall of assets is generally the route that is chosen, to pierce the corporate veil and trigger the director and/or shareholder liability of a French limited liability company. However, there is numerous French case law, showing that French courts do not hesitate to hold French **and** foreign parent companies liable for the debts of French subsidiaries, especially in case of abuse of corporate veil, by way of intermingling of estates, either by intermingling of accounts or abnormal financial relations. This usually leads to the extension of insolvency proceedings, in case of intermingling of estates, but could also trigger the director and/or shareholder liability in tort for gross misconduct.

Indeed, if a shareholder has committed a fault or gross negligence that contributed to the insolvency of, and subsequent redundancies in, the French subsidiary, that shareholder may be liable to the employees directly. Pursuant to recent French case law, the shareholder could be held liable in the event its decisions:

- hurt the subsidiary;
- aggravate the already difficult financial situation of the subsidiary;
- have no usefulness for the subsidiary, or
- benefit exclusively to the shareholder.

Of course, any French court decisions are relatively easily enforceable in any other European Union ("**EU**") member-state, such as the UK, thanks to the EU regulation 1215/2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. This regulation allows the enforcement of any court decision published in a EU member-state without any prior exequatur process. Therefore, the foreign parent-company will not be protected by the mere fact that it is located in the UK, for example, as opposed to France: it will be liable anyway, and the French courts' judgments will be enforceable in the UK against it. Moreover, a new international convention, the Hague convention on the recognition and enforcement of foreign judgments in civil or commercial matters was concluded, on 2 July 2019, which will become a 'gamechanger' once it becomes ratified by many countries around the world, included the EU. It will therefore become even easier to enforce French court decisions in third-party states, even those located outside the EU.

So what is the best route to restructure or wind up the French operations of your creative business, if so much is at stake?

## 1. How to lawfully terminate your French lease

Most French commercial operations are conducted from commercial premises, be it a retail outlet or some offices. Therefore, leases of such commercial spaces were entered into with French landlords, at the inception of the French operations.

How do you lawfully terminate such French leases?

Well, it is not easy, since the practice of "locking commercial tenants in" has become increasingly common in France, through the use of pre-formulated standard lease agreements which impose some onerous obligations on commercial tenants, that were not subject to any negotiation or discussion between the parties.

This evolution is rather surprising since France has a default regime for commercial leases, set out in articles L. 145-1 and seq. of the French commercial code, which is rather protective of commercial tenants (the "Default regime"). It defines the framework, as well as boundaries between, the landlord and its commercial tenant, as well as their contractual relationship.

For example, article L. 145-4 of the French commercial code sets out that, in the Default regime, the term of the lease cannot be lower than nine years. Meanwhile, articles L. 145-8 and seq. of the French commercial code describe with minutia the Default regime to renew the lease after its termination, declaring null and void any clause, set out in the lease agreement, which withdraws the renewal right of the tenant, to the lease agreement.

But what does the Default regime say about the right of a tenant to terminate the lease? Nothing, really, except from articles L. 145-41 and seq. of the French commercial code, which provide that any clause set out in the lease agreement in relation to the termination of the lease will only apply after one month from the date on which a party to the lease agreement informed the other party that the latter had to comply with all its obligations under the lease agreement and, should such request to comply with its contractual obligations be ignored, the former party will exercise its right to terminate the lease agreement within a month. However, in practice, it is very difficult for French commercial tenants to invoke such articles from the French commercial code, and subsequently prove that their landlords have not complied with their contractual obligations under the lease. This is because such French lease agreements often set out clauses that exonerate the landlords from any liability in case the premises are defective, obsolete, suffer from force majeure cases, etc.

To summarise, the Default regime does not provide for any automatic right for a commercial tenant to terminate the lease agreement, for any reason. It is therefore advisable, when you negotiate the clauses set out in such lease agreement, to ensure that your French entity (be it a branch or a French limited liability company) has an easy way out of the 9 years' lease. However, since the balance of power is heavily skewed in favour of commercial landlords – especially for sought-after retail locations such as Paris, Cannes, Nice, and other touristic destinations – there is a very high probability that the landlord will dismiss any attempts made by the prospective commercial tenant to insert a clause allowing such tenant to terminate the lease on notice, for any reason (i.e. even in instances when the commercial landlord has complied with all its obligations under the lease).

Still included in the Default regime, on the topic of termination of leases, is article L. 145-45 of the French commercial code, which sets out that the institutionalised receivership or liquidation (i.e. "redressement ou liquidation judiciaires") do not trigger, in their own right, the termination of the lease relating to the buildings/premises affected to the business of the debtor (i.e. the tenant). Any clause, set out in the lease agreement, which is contradictory to this principle, is null and void, under the Default regime. While this article sounds protective for commercial tenants, it also infers that there is no point in placing the tenant's business in receivership or liquidation, to automatically trigger the termination of the lease. Such a situation of court-led receivership or liquidation of the French entity will not automatically terminate the lease of its premises.

Consequently, the most conservative way out may be to wait the end of the nine years' term, for a commercial tenant.

In order to have more flexibility, many foreign clients that set up French commercial operations prefer to opt out of the Default regime, which imposes a nine years' term, and instead enter into a dispensatory lease ("bail dérogatoire") which is not covered by the Default regime.

Indeed, article L. 145-5 of the French commercial code sets out that "t*he parties can (…) override*" the Default regime, provided that the overall duration of the commercial lease is not longer than three years. Dispensatory leases, which have an overall duration no longer than 3 years, are therefore excluded from, and not governed by, the Default regime set out in articles L. 145-1 and seq. of the French commercial code, and are instead classified in the category of "contrats de louage de droit commun" i.e. civil law ordinary law contracts of lease, which are governed by the provisions set out in the French civil code, relating, in particular, to non-commercial leases (article 1709 and seq. of the French civil code).

Therefore, if a foreign parent negotiates a dispensatory lease for its French operations, it will be in a position to call it a day after three years, instead of nine years. However, it will not be able to benefit from the tenants' protections set out in the Default regime and will therefore need to negotiate very astutely the terms of the commercial lease with the French landlord. It is therefore essential to seek appropriate legal advice, prior to signing any lease agreement with any French landlord, in order to ensure that such lease agreement offers options, in particular, for the tenant to terminate it, in case of contractual breaches made by the landlord, and, in any case, upon the end of the three years' term.

The tenant should keep a paper trail and evidence of any contractual breaches made by the landlord during the execution of the lease, as potential "ammunition" in case it decides to later trigger the termination clause under the lease agreement, for unremedied breach of contract.

## 2. How to lawfully terminate your French staff

Once the termination of the lease agreement is agreed, it is time for the management of the French operations to focus their attention on termination the employment agreements of French staff members (the "**Staff**"), which can be a lengthy process.

An audit of all the employment agreements in place with the Staff  should be conducted, confidentially, before making a move, in order to assess whether such agreements are "contrats à durée indéterminée", or "**CDI**" (i.e. indeterminate duration employment agreements) or "contrats à durée déterminée", or "**CDD**" (i.e. fixed term employment agreements).

As part of this audit, the legal and management team should clarify the amount of the sums due to each member of the Staff, relating to:

- any paid leave period owed to her;
- in case of CDDs, if no express agreement is signed by the member of Staff and the employer upon termination, all outstanding remunerations due during the minimum duration of the CDD;;
- in case of CDDs, an end of contract indemnity at a rate of 10% of the total gross remuneration;
- in case of CDIs, any notice period salary owed to her;
- in case of CDIs, any severance pay owed to her and
- any outstanding social contributions on salary.

This audit will therefore enable the French business, and its foreign parent-company, to assess how much this Staff termination process may cost.

In France, you cannot terminate Staff at will: you must have a "lawful" reason to do so.

Justifying the termination of a CDD ahead of its term may be pretty complex and risky, in France, especially if the relevant members of Staff have behaved in a normal manner during the execution of such CDD, so far. It may therefore be worth for the employer to pay all outstanding remunerations due during the minimum duration of the CDD, in order to avoid any risk of being dragged to any employment tribunal, by such members of Staff.

As far as CDIs are concerned, there are three types of termination of CDIs, as follows:

- "licenciement pour motif économique" (i.e. layoff for economic reasons);
- "rupture conventionnelle du CDI" (i.e. mutually agreed termination of the employment agreement);
- "rupture conventionnelle collective" (i.e. collective mutually agreed termination of the employment agreement).

A "licenciement pour motif économique" must occur due to a real and serious economic cause, such as job cuts, economic difficulties of the employer or the end of the activity of the employer.

This option would therefore be a good fit for any French entity that wants to stop operating in France. It does come with strings attached, though, as follows:

- the employer must inform and consult the "représentant du personnel", or the "Comité d'entreprise";
- the employer asks the relevant Staff to attend a preliminary meeting and notifies them of the termination of their CDIs as well as the reasons for such termination;
- the employer sends a termination letter to the relevant Staff, at least 7 business days from the date of the preliminary meeting, or at least 15 business days from the date of the preliminary meeting if such member of Staff is a "cadre" (i.e. executive), which sets out the economic reason which caused the suppression of the job occupied by the employee, the efforts made by the employer to reclassify the employee internally, the option for the employee to benefit from reclassification leave and
- the employer informs the French administration, i.e. the relevant 'Direction régionale des entreprises, de la concurrence, de la consommation, du travail et de l'emploi' ("**DIRECCTE**") of the redundancies.

Another route to lawfully terminate the Staff is via a "rupture conventionnelle du CDI", i.e. mutually agreed termination of the employment agreement. This is only open to French operations where the Staff is ready to cooperate and mutually agree to the termination of its employment agreements. This situation is hard to come by, in reality, to be honest, by why not?

If the French entity manages to pull this off, with its Staff, then the "convention de rupture conventionnelle" must be signed, then homologated by the DIRECCTE, before any employment agreement is officially terminated.

If the DIRECCTE refuses to homologate the convention, the relevant Staff must keep on working under normal conditions, until the employer makes a new request for homologation of the convention and … obtains it!

Finally, in case an "accord collectif", also called "accord d'entreprise", was concluded in the French company, then a "rupture conventionnelle collective" can be organised. If so, only the Staff who has agreed in writing to the "accord collectif" can participate to this collective mutually agreed termination of its employment agreements.

It’s worth noting that French employees are rather belligerent and often file claims with employment tribunals, upon termination of their employment agreements. However, the Macron ordinances, which entered into force in September 2017, have set up a scale that limits the maximum allowances which could be potentially be paid to employees with minimal seniority, in such employment court cases. Thus, employees having less than one year’s seniority are allowed to collect a maximum of one month of salary as compensation. Afterwards, this threshold is grossed up by more or less one month per year of seniority up to eight years. However, such scale does not apply to unlawful dismissals (those related to discrimination or harassment) or to dismissals which occurred in violation of fundamental freedoms. While many French lower courts have published judgments rejecting such Macron scale, the “Cour de cassation” (i.e. the French supreme court) validated such Macron scale in July 2019, forcing French employment tribunals to comply with such scale.

While this should come as a relief to foreign parent companies, it is worth noting that the more orderly and negotiated the departure of the Staff, the better. Having to fight employment lawsuits in France is no fun, and can be cost and time intensive. They therefore must be avoided at all cost.

## 3. How to restructure your creative business in France: terminate other contracts with third parties and clean the slate with French authorities

Of course, other contracts with third parties, such as suppliers, local service providers, must be lawfully terminated before the French operations are shut down. The takeaway is that the French entity and its foreign parent company cannot leave a chaotic and unresolved situation behind them, in France.

They must terminate and lawfully sever all their contractual ties with French companies and professionals, before closing shop, in compliance with the terms of any contracts entered into with such French third parties.

Additionally, French companies must pay off any outstanding balances due to French authorities, such as the French social security organisations, the URSSAF, and the French tax administration, before permanently closing down.

## 4. How to restructure your creative business in France: you must properly wind up your business

Once all the ongoing obligations of the French operations are met, by lawfully terminating all existing agreements such as the commercial lease, the employment agreements, the suppliers’ agreements and the service providers’ agreements, as discussed above, it is time to wind up your business in France.

French limited liability companies have two options to terminate their business as an ongoing concern due to economic grounds, i.e. proceed to a “cessation d’activité”.

The first branch of the alternative is to execute a voluntary and early termination of the French business as an ongoing concern. It can be exercised by the French company, its shareholders and its board of directors, when it can still exercise its activity and pay back its debts. If the articles of association of such French company provide for the various cases in which the company may be wound up, such as the end of the term of the French company, or upon the common decision made by its shareholders, then it is possible for the French limited liability company and its directors to execute a voluntary and early termination of the business as an ongoing concern.

The second branch to the alternative, opened to French limited liability companies, occurs when a company cannot pay its debts anymore, and is in a situation of "cessation de paiements" i.e. it cannot pay its debts with its assets, in cessation of payments. In this instance, the French company must file a notification of cessation of payments with the competent commercial courts within 45 days from the date on which it stopped to make payments. Also, within that time frame of 45 days, the board of directors of the French company must open a "procédure de redressement ou de liquidation judiciaire" (i.e. receivership or liquidation institutionalised process, monitored by French courts) with the competent commercial court. This court will decide, further to examining the various documents filed with the "déclaration de cessation des paiements", which institutionalised process (receivership? liquidation?) is the most appropriate, in view of all the interests that need being taken into account (debts, safeguarding employments, etc.).

If you want to exit the French territory in a graceful manner, you do not want to find yourself in a situation of cessation of payments, and then receivership or liquidation monitored by French courts. Not only this guarantees a protracted and painful judiciary process to terminate your French operations, but this may lead to situations where the money claims made against the French company would be escalated to its shareholders, directors and/or parent company, as explained in our introduction above.

Not only the parent company, and any other shareholder, could be dragged in the mud and found liable, but its directors, and in particular its managing director, too. French commercial courts have no patience for sloppy and irresponsible management, and many managing directors ("associes gerants") have seen their civil liability triggered because their actions had caused some prejudices to the French company or a third party. Even criminal liability of an "associe gerant" can be triggered, in case the French court discovers fraud. In particular, it is frequent that in collective insolvency proceedings, if the judicial liquidation of a French limited liability company shows an asset shortfall ("insuffisance d'actif"), the courts order its managing director to pay, personally, for the company's social liability, if she has committed a management error.

To conclude, the French company acts as a shield for its managing director, except if such director commits a personal mistake detachable from her mandate, in case the company is still solvent. However, if the company is in receivership, both the shareholders', and the directors' liability may be triggered in many ways, by French courts, the French social security contributions entity URSSAF and the French tax administration.

It is therefore essential to leave France with a clean slate, because any unfinished business left to fester may hit your foreign company and the management like a boomerang, by way of enforceable and very onerous French court decisions.

Don't worry, though, we are here, at Crefovi, to service you to achieve this, and you can tap into our expertise to leave French territories unscathed and victorious.

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