

Pratt's Journal of Bankruptcy Law

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Steven A. Meyerowitz

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France Introduces New Legal Regime for Security Agents in Debt Financings

By *Lionel Dechmann, Xavier Farde, Etienne Gentil, and Michel Houdayer**

Syndicated financings with French security have adopted the new regime for security agent appointment. The new regime establishes a legally straightforward and simplified system for a security agent to hold security on behalf of multiple secured parties and provides practical and legal advantages over parallel debt and related mechanisms developed to date. The authors of this article discuss the new legal regime.

A new “agent des sûretés” (security agent) regime has been introduced under French law and came into effect on October 1, 2017.¹ New articles 2488-6 to 2488-12 of the French Civil Code provide, for the first time, a legally straightforward, reliable, and practical foundation under French law for a security agent to hold and (as the case may be) enforce French security on behalf of multiple secured parties.

By way of background, security for European debt financings featuring multiple secured parties (such as secured syndicated loan agreements) is usually granted in favor of a common security agent appointed by the secured parties as trustee, to receive, hold, and manage the transaction security for their benefit. Common law systems, such as English or New York law, recognize this concept of trust.

France, like many other civil law systems, does not recognize the concept of trust (except in limited respects), and as a result, secured parties have, until now, required different mechanisms to deal—in a not entirely satisfactory way—with French security.

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¹ Ordonnance n° 2017-748 of 4 May 2017, pursuant to authority under Article 117 2° of law n° 2016-1691 dated 9 December 2016 known as the “Sapin 2” law.

CURRENT FRENCH LAW PRACTICE IN FRENCH LAW GOVERNED SYNDICATED FINANCINGS

French law governed syndicated financings have traditionally used agency mechanisms in which the security agent acts solely as agent for the finance parties. The finance parties are the direct beneficiaries of the security interest, requiring the security agent to identify and list all the beneficiaries of the security at the start of the transaction, and every time new security is granted. This mechanism does accommodate transfers by the secured parties (*i.e.* the security follows assignments/transfers of the secured debt without further action), but implementing the mechanism can be cumbersome.

Practical issues also arise when a French security grantor is subject to safeguard or insolvency proceedings, because each secured party is required to claim for itself in the proceedings unless, at the time, the security agent is specially granted a power of attorney by each of the secured parties it is to represent in the proceedings (note that this special power of attorney would be in addition to the general powers of attorney provisions in favor of the security agent in intercreditor or other security documents).²

To deal with some of these issues, the concepts of fiduciary transfers of ownership (*fiducie*) and fiduciary grants of security interest (*fiducie-sûreté*) were introduced in the French Civil Code in 2007.³ Unfortunately, the technical conditions, administrative burdens, and associated costs have resulted in financing parties largely ignoring these legal tools, except in certain restructuring situations where such legal tools are extremely useful and effective. Also in 2007 an “agent des sûretés” (security agent) mechanism was introduced in the French Civil Code,⁴ but the mechanism’s numerous shortcomings were such that it was also ignored by practitioners.

CURRENT FRENCH LAW PRACTICE IN FOREIGN LAW GOVERNED INTERNATIONAL SYNDICATED FINANCINGS

To date, French law security for international syndicated financings has often been granted directly to a foreign law security agent, using so-called parallel debt constructs governed by English, New York, or other foreign law. Parallel debt is a construct under which each obligation owed to a given secured party

² Article L622-24 of the French Commercial Code.

³ Articles 2011 to 2030 of the French Civil Code.

⁴ Article 2328-1 of the French Civil Code introduced by law 2007-211 dated 19 February 2007.

in the financing is also independently (and in parallel) owed to the security agent. The French law security will often secure each secured party (raising the issues referred to above) as well as the security agent's rights under the parallel debt.

In the landmark *Belvédère* ruling in 2011,⁵ the French Cour de Cassation (Supreme Court) recognized the validity of the foreign law parallel debt and the rights of the security agent to claim (in its own right) as a parallel debt creditor, provided this claim did not lead to the risk of the French borrower or guarantor being liable to pay twice for the same underlying obligation.

Although the parallel debt mechanism presents secured parties with the disadvantage that it exposes them to the risk of a security agent's insolvency, the recognition of its validity in the *Belvédère* ruling has resulted in security agents being appointed under foreign law governed finance documents debt so as to receive foreign law parallel creditor rights (secured by French law security) in a way that is not available to security agents appointed under French law governed finance contracts.

THE NEW FRENCH SECURITY AGENCY REGIME

A security agent can now hold guarantees and security interests granted directly to the security agent, and it can register, manage, and enforce the security interests in its own name on behalf of the secured creditors.⁶ The security agent is expressly authorized by law to take all necessary steps and proceedings (in its own name) relating to the secured assets and rights, including to prove claims in insolvency or safeguard proceedings (without the need for a special power of attorney granted by each secured creditor of the kind referenced above).

A further major advantage of this regime is that the security in the rights and assets granted in favor of the security agent, and the proceeds of enforcement of the security, are ring fenced from the rest of the security agent's assets and liabilities.⁷ This is a very novel approach for French law, which is generally hostile to carving out any part of a debtor's assets for the benefit of any group of creditors.

⁵ Cass. Com, 13 September 2011, n° 10-25.333, 10-25.731, 10-25.908, Bulletin 2011, IV, n° 131.

⁶ Article 2488-6 of the French Civil Code.

⁷ Article 2488-6, alinéa 3 of the French Civil Code. Whether this ring fencing provided under French law will be respected in the event of an insolvency proceeding for a security agent under a foreign law will be determined by choice of law rules that are difficult to predict in advance.

Other key features of this new regime include:

- The rights and assets acquired by the security agent when exercising its role as security agent may be seized only by persons who have acquired rights against the security agent in connection with the management and safekeeping of the assets.⁸
- Safeguard, insolvency, or liquidation proceedings affecting the security agent are ineffective vis-à-vis these segregated assets and rights.⁹
- The parties may freely agree to the terms upon which a security agent may be replaced,¹⁰ any such replacement transferring, as a matter of law and without any formalities being required, the segregated assets and rights to the successor security agent.¹¹
- Finally, the security agent will be liable on agreed contractual terms for breach of contract and negligence in the performance of its duties as security agent, although claims for this liability will not be exercisable against the collateral it holds as security agent.¹²

Procedurally, the document appointing the security agent must expressly state that the security agent is appointed as an agent des sûretés under Articles 2488-6 to 2488-12 of the French Civil Code, as well as expressly state the purpose and the duration of the security agent's appointment.¹³ The appointing document does not need to be the debt or security instrument itself, so the appointment can be made by the secured parties in an intercreditor agreement (as is typically the case in senior/second lien/mezzanine or high yield/super senior revolving credit facility transactions). Finally, the security agent must specify that it is acting as security agent on behalf of the creditors each time it acts in such capacity.¹⁴

THE WAY FORWARD

Given that the new regime is more robust than any of the previously available alternatives for French security in syndicated transactions, practitioners will likely widely embrace the new regime now that it has come into force.

⁸ Article 2488-10, alinéa 1 of the French Civil Code.

⁹ Article 2488-10, alinéa 2 of the French Civil Code.

¹⁰ Article 2488-11, alinéa 1 of the French Civil Code.

¹¹ Article 2488-11 of the French Civil Code.

¹² Article 2488-11 of the French Civil Code.

¹³ Article 2488-7 of the French Civil Code.

¹⁴ Article 2488-8 of the French Civil Code.

Absent other reasons, it is expected that secured parties will include the relevant language to facilitate this regime in secured financings that include French security and which close on or after October 1, 2017. Because the new regime must be elected for a given grant of security at the time of grant, it was not available for French security being granted before October 1, 2017. And because there would be practical difficulties in regulating the administration of a mixed French security package (in which some of the security predates the regime and other parts follow the new regime) it is expected that (barring special circumstances) the new regime likely will not be added for new security (granted on or after October 1, 2017) on existing deals that already have French security, including deals that closed in the interim period before October 1, 2017.

The parallel debt construct will no longer be needed in non-French law governed financing transactions in relation to French security, and parties should include a French law governed section in the relevant (English, New York, or other foreign law governed) intercreditor or similar agreement, providing for a special security agent appointment under Articles 2488-6 to 2488-12 of the French Civil Code. Ideally, security agent replacement provisions should also take into account the flexibility afforded in respect of the French law security agent appointment.

We expect French law governed syndicated financing transactions to adopt the new regime. If these financings are also secured by non-French security interests, parties may require local legal advice to determine whether local law will recognize and give effect to the rights of a French law appointed security agent. It would be surprising if jurisdictions that recognize trust relationships or parallel debt constructs refuse to give effect to the new French law security regime.

Finally, new French law governed security documents will need minor adaptation so that the security is granted only to the security agent acting in this new capacity, but this new regime should simplify the grant and management of these security interests over time.