Reform of the French "Civil code"

Catherine Ottaway and Georges-Louis Harang write on the Insolvency law and Contract law in the light of the Reform of the French "Civil code" entering into force on 1 October 2016

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After years of discussions, the chapter related to the "Contract", included in the Civil code (the "Code") since 1804, has been entirely and substantially reformed by the Ordinance[1] dated 10 February 2016 (the "Reform").

The purpose is to improve the French contract law in order to:

(i) introduce most of the case law developed these past decades so that the code reflects the substantive law (called the "codification");
(ii) modernise the contract law so as to reinforce its economic efficiency and its attractiveness; and
(iii) introduce new concepts in the contract law as far unknown under French civil and commercial law.

As a result, all the articles governing the "contract" in the Code are modified, not only their numbering (to organise it into a more coherent body of law), but also their content.

New articles have been drafted and the new legislation will enter into force on 1 October 2016. Nevertheless, the contracts signed before 1 October 2016 will still be submitted to the previous Contract law, which means that during the next years two different legislations will apply.

Among the (r)evolutions, without being exhaustive, the Reform

(i) admits the unforeseeability doctrine,
(ii) introduces in the Code the concept of significant imbalance between the rights and obligations of the parties (in a standard contract and not anymore only in the Consumer code), or
(iii) does away with previous concepts (like the doctrine of "cause", a key feature of the traditional French contract law).

Practitioners will therefore face a new challenge in their day to day practice.

This Reform might impact the other legal fields given that the civil law permeates all the kinds of law. We might expect some interference with the insolvency law too, especially regarding one of the main innovation of the Ordinance, which is the introduction of the "*théorie de l'imprévision*", the "*unforeseeability doctrine*", in the Code.

The recognition of the unforeseeability doctrine in Civil law

The *Cour de cassation* (French High Court) refused to adapt, revise or terminate a contract so far because of an imbalance resulting from a sudden change – not foreseen by the parties – in the economic conditions that existed at the time of the conclusion of the contract, on the ground that the unforeseeability doctrine conflicts with the principle enshrined in the current Article 1134 of the Code according to which agreements lawfully entered into have the force of law for those who have made them.

The Reform puts the French civil system into a new age of the binding force of contracts as the parties will be allowed to renegotiate the contract when unpredictable circumstances occur and to insert in their contract a hardship clause[2] in order to organise the conditions of this renegotiation. Therefore, the parties will be able to challenge the binding force of their contract, except for the existence of a contrary clause.

The new Article 1195 of the Code provides that:

"*If a change of circumstances, unforeseeable at the time of the conclusion of the agreement, renders its performance excessively onerous for one party, who did not accept to bear such risk, that party can request renegotiation of the agreement from the other party. The requesting party continues to perform his obligations during the renegotiation period. In the case of refusal or failure of the renegotiation, the parties may agree to rescind the agreement, upon the date and conditions they determine, or together request the judge to proceed with its revision. Failing agreement within a reasonable period of time, the judge may, at the request of one of the parties, revise the agreement or terminate it at the date and under the terms and conditions he fixes himself.*"

The change is fundamental, as the previous principle was the non-interference of a judge in the contract. As of 1 October 2016 a judge will be able to interfere in the contract signed after this date.

In fact, as of 1 October 2016, a contract might be revised or terminated due to unforeseen circumstances that make it too onerous for one party to meet its obligations. Parties which cannot agree on this can now ask a judge to adapt or terminate a contract. Parties might also forbid, in their

contract, hardship clauses to prevent such eventuality from happening and thus, to maintain the binding force of their contract in any circumstances.

May this innovation interact with some insolvency proceedings and, if so, change the rules governing such proceedings?

The potential impacts of the unforeseeability doctrine on the safeguard proceedings

Among the different proceedings related to bankruptcy and concerning their implementation conditions, we may wonder about whether the Reform and the unforeseeability doctrine might have an impact within the context of safeguard proceedings (article L 620-1 of the Commercial code).

The safeguard proceedings may be opened by the Commercial court:

"*[…] at the request of the debtor mentioned in Article L. 620-2, who can prove that although he/she is not faced with a cessation of payments,* ***he/she has difficulties that he/she is unable to overcome****. The purpose of this procedure is to facilitate the reorganisation of the business in order to allow the continuation of the economic activity, the maintenance of employment and the settlement of liabilities. […]*" (emphasis by us)

Therefore, the unpredictable circumstance or onerous circumstance (economical difficulty) to which one party could not face is the only condition provided for in both new article 1195 and article L 620-1.

Where the main difficulties of a company come from a contract, the potential defaulting company will now have to choose an option:

- Try to renegotiate the contract, under the Judge's supervision, if necessary, without the prejudice of the termination of the contract; or
- Request the opening of safeguard proceedings and the opportunity to benefit from imperative rules, such as the stop of any claim and the continuation of the contracts in force.

Which one should prevail?

Authors[3] are trying to develop arguments in favour and against one kind of proceedings rather than the other, arguing the following:

- In case of a hardship clause, parties have contractually provided the possibility to renegotiate the contract and, due to this, only the way of the revision of the contract should be allowed in case of economic difficulties, not the safeguard proceedings (should the company not be in default of payment);
- the choice between Article 1195 or Article L 620-1, in case of economic difficulties, should belong to the co-contractant facing difficulties. This choice is necessary as the period to undertake actions under Article 1195 or Article L 620-1 is different. Safeguard proceedings will be opened rapidly if the conditions are fulfilled, whereas the revision of the contract under Article 1195 will take time, as the parties will have to discuss and to find a

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IS THERE A RISK OF A DIVERSION OF THE SAFEGUARD PROCEEDINGS?

deal, or to seize a Judge, and that could take months before reaching a decision. The consequences might be important as, without a fast opening of safeguard proceedings, a company could be deemed in a state of default of payment and, thus, excluded from any of the measures implied by the reorganisation of the business.

Furthermore, is there a risk of a diversion of the safeguard proceedings? Will the party in economical difficulty try to pressure its co-contractant to renegotiate the contract by threatening the other party with the opening of safeguard proceedings?

More than a way to be protected by safeguard proceedings and its imperative rules in order to reorganise its business, the co-existence of the safeguard proceedings and the unforeseeability doctrine, grounded on the same conditions, might be an argument of negotiation, by using the first one to the benefit of the second.

However, where the renegotiation provided by the Reform will be semi-confidential (between the parties and possibly, implying a judge), the safeguard proceedings are known publicly and this can lead to other difficulties.

This potential disadvantage could be limited by using, in a first time, the "*mandat ad-hoc*" proceedings, which are in fact a confidential mediation between the parties, with the assistance of an insolvency office holder appointed by the Commercial Court.

Conclusion

Will the Reform be likely to challenge the bankruptcy-prevention proceedings and the way all the practitioners dealt with this specific law until today?

Given that the new articles of the Code are definitively drafted, the interactions between the "new" contract law and the insolvency law can now be seriously considered, especially regarding the unforseeability doctrine, although case law will define and limit these interactions in the near future. ■

Footnotes:

1 Act adopted without any in-depth scrutiny by the Parliament.
2 Only admitted before in international contracts.
3 For example, see the article by Philippe Delebecque, in Bulletin Joly *Entreprises en Difficulté*, 1 May 2016, n° 3, page 209.