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Practice Group:
**Bankruptcy and
Restructuring**

Continuation of contracts under an insolvency proceeding governed by French law: Better be short!

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When a company is in good standing and healthy, the question of the renewal of a contract or its duration arises only in a competitive environment. In case of an insolvency proceeding, the situation is more complex, notably for suppliers whose payment remains uncertain. If challenging the decision taken by the judicial administrator imposing the continuation of a contract has little chance of success, one solution may lie in the nature and the terms of the original contract.

When a company is under an insolvency proceeding, the judicial administrator is entitled by law to decide, to the exclusion of any other parties, whether or not a contract should be terminated. The judicial administrator could therefore force a co-contractor to perform the contract entered into with the bankrupted company if the contract was entered into before the opening of an insolvency proceedings. The decision of the administrator to impose the performance of a contract is binding among all parties regardless of the status of the insolvency proceedings (e.g. Article L. 622-13, II, para. 1 of the French Commercial Code provides such power to the administrator in the event of a safeguard proceeding or a reorganization proceeding and Article L. 641-11-1, II, paragraph 1 of the French Commercial Code in the event of a liquidation proceeding).

The decision to pursue a contract may be challenged by the co-contracting party. The recourse against such decision being extremely limited, the co-contractor is left powerless and has no other choice than to accept such decision, decision taken to preserve the business of the company.

The current economic turmoil is forcing companies whose cash flow is stretched to attempt to protect themselves against the risk of having to maintain business relationship with companies in poor financial health. Certain foreign laws are more flexible than French law by allowing parties to insert in their agreement a provision preventing such risk, so that the parties are automatically released from their contractual obligations as soon as a party files for bankruptcy.

In France, the automatic termination of a contract due to the insolvency proceedings of a party is to be excluded straight away. The invalidity of such provision is provided for by law and constantly confirmed by case law, leaving no room for any alternative interpretation.

In this context, what can be suggested to French or foreign companies entering into a contract governed by French law to protect themselves against a risk of defaulting payments without however jeopardizing their business relations?

If the solution cannot come from private negotiation, it actually lies in the limits of the powers granted to the judicial administrator.

Indeed, the administrator is entitled by law to impose the continuation of a contract during the insolvency proceedings under the same conditions but he has no power to force its renewal after the end of its term. In this context, a distinction should be made between two scenarios depending on whether or not a commercial contract has a limited or unlimited duration:

First scenario: In the event of an indefinite term contract, the judicial administrator may impose the continuation of the contract - this decision being effective until the end of the insolvency proceedings - the judicial administrator therefore preventing any unilateral termination by the co-

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contractor. In this case, the party *in boni* is compelled to perform its obligations until the end of the insolvency proceedings.

Second scenario: In the event of a fixed term contract, the judicial administrator may also request the continuation of the contract, but he will not be in a position to impose its renewal when it comes to an end. The party *in boni* shall therefore freely decide not to renew the contract and is thus entitled to limit, *a posteriori*, the decision of the judicial administrator not to terminate the contract.

The power granted by law to the judicial administrator shall be regarded as a power to impose the continuation of a contract and not as a power to extend the contract beyond its initial duration without obtaining a new agreement from the co-contracting party.

Eager not to be bound to a company which it knows to be in poor financial health, a co-contracting party may have interest in entering into short-term contracts, even at the risk of having to renew the contract on a higher frequency, in order to be able to move out from a contract entered into with a company under a French insolvency proceedings.

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