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The *fiducie-sûreté*: the most effective French security interest?

The *fiducie* has been the subject of increased interest by lenders over the past few years in France. Even though there is no significant case law supporting this, some academics have gone so far as to refer to this mechanism as “the queen of securities”.

The *fiducie*, introduced following years of debate into French law by a law dated 19 February 2007², is directly inspired by the English trust mechanism, initially created to protect the land ownership while the land owners were away fighting in the Holy Land. The *fiducie* can be divided into several categories:

- The *fiducie-gestion* which consists of the transfer of assets by the settlor (“*le constituant*”) to the trustee (“*le fiduciaire*”) in order for the latter to manage such assets;
- The *fiducie-libéralité*, used to donate an asset to a given beneficiary, which remains prohibited under Article 2013 of the French Civil code; and
- The *fiducie-sûreté* (hereafter the “***fiducie***”) which allows temporary transfer of ownership and title of specifically identified assets, rights or security interests, existing or future, belonging to a debtor or a third party, to a separate estate created for the purposes of the *fiducie* for as long as monies are owed by the debtor to the creditor. These assets (hereafter the “***fiducie assets***”) are managed by the *fiduciaire* for the benefit of the beneficiary(ies)³. The *fiducie* is an innovative mechanism under French law as the trustee segregates the *fiducie* assets from his personal estate - French law had, up to the creation of the *fiducie*, prohibited the possibility for a person (physical or legal) to have several estates.

The three main advantages of the *fiducie* are the following:

- First, creditors benefit from the maximum protection due to the exclusive nature of the property right that the *fiducie* confers to its beneficiary(ies) (who would normally be the creditor(s) of the settlor);

- Second, this form of security requires, alongside other conditions (**section 1**), a written contract which can be, and often is, tailored specifically to each transaction and circumstances. Unlike other French security interests, the *fiducie* leaves room to a certain amount of creativity at the drafting stage. As a consequence, the *fiducie* may be a rather complex document to draft, depending on the structure and context of the transaction (**section 2**), which may impact the cost and hence its ability to be used on smaller transactions;
- Finally, the use of a *fiducie* offers an advantageous regime to creditors in various insolvency scenarios (**section 3**).
- In recent times, the use of the *fiducie* has increased due to several reforms implemented since its creation⁴. It has also been made more attractive for both borrowers and lenders as the 2014 Amending Budget Law⁵ modified the *fiducie*'s tax treatment, which was previously considered as unsuitable (**section 4**).

1. Creation – Key Conditions

- The settlor and the beneficiary can either be natural persons or legal entities without any specific restrictions.
- The trustee may only be a credit institution, an investment services provider or an insurance company. Since February 2009⁶, lawyers qualified to practice as “*avocats*” are also authorized to act as trustees.
- Certain mandatory provisions must be included in the *fiducie* agreement⁷ (e.g., the determination of the assets transferred or, for future assets, elements permitting their identification; the term of the *fiducie*, not exceeding 99 years; the identity of the settlor, the trustee and the beneficiary (if the identity of the latter is not yet determined, the agreement must provide rules governing identification); the terms of the trustee's appointment; the determination of the debt guaranteed by the *fiducie* as well as an estimated value of the secured assets⁸).
- The *fiducie* agreement creating the *fiducie* and any document attached must be registered with the French tax authorities, against a €125 flat registration fee, within one month of its date of

execution, failing which it will be deemed to be null and void.

- The main features of the *fiducie* agreement are also filed with the *Registre National des Fiducies*⁹. The ability to consult this register is solely limited to certain persons *i.e.*, the public prosecutor, tax and customs agents and law enforcement officers.

2. The *fiducie* agreement in practice

The agreement governing the *fiducie* can be a rather complex document to draft, mostly due to the innovation of this mechanism and the contractual flexibility granted to the parties. Apart from certain legal provisions that are required by French law, some other provisions, inspired by standard provisions found in Common law trust agreements, may be worth considering in the *fiducie* agreement:

- The scope of the trustee's appointment will need to be determined in particular detail by the agreement. The latter may include a number of general representations from the trustee, such as not being subject to any insolvency proceedings, or in the midst of the "*période suspecte*"¹⁰, adequate insurance and the required qualifications to act in such capacity, but also a number of specific covenants depending on the nature of the secured assets and the term of the agreement.

For instance, for the transfer of real estate assets to the *fiducie*, the agreement will need to govern the management of such assets. If the trustee is entrusted this role, the initial purpose of the *fiducie* will be extended to include *fiducie gestion* provisions. The agreement will also need to determine who is the recipient of any invoice and to what extent the trustee, if he is assigned that mission, distributes them to the beneficiary(ies).

If the assets placed in *fiducie* are shares, it will be essential to determine how the trustee or his appointed agent will vote at the shareholders' meetings and report to the beneficiaries prior to and after these meetings; which representations and warranties will be made by the trustee in case of a sale of the shares and how and by whom the sales process will be driven; how the revenues will be distributed amongst the beneficiaries. Generally, there will also be a

series of duties provided for in the agreement such as positive and negative obligations.

- As per the French Civil code, the trustee is liable, on his own personal estate, for the faults he may commit in the course of his appointment¹¹. Notwithstanding this liability, specific provisions may be inserted in the agreement at the trustee's request. For instance, in the event a third party takes legal action against the trustee in relation to the assets transferred to the *fiducie* by the settlor, the latter or another party to the agreement would indemnify the trustee for all related liabilities and expenses arising from this claim and also assist the trustee in the procedure.
- The replacement of the trustee may be requested, according to the French Civil code, by the beneficiary(ies), the settlor or by the trustee himself¹² in the event the latter fails to comply with his obligations, jeopardizes the assets placed under the *fiducie*, or is subject to certain insolvency proceedings¹³. A specific provision may be required to address this in further detail.
- Article 2017 of the French Civil code also provides that the settlor may, at any time appoint a third party, empowered with the same powers as the settlor, in order to ensure that his interests are properly considered throughout the term of the agreement. This ability may be excluded from the *fiducie* agreement by the settlor.
- Finally, a confidentiality provision covering the information and provisions of the *fiducie* agreement will be important. Notwithstanding such a provision, a *fiducie* agreement is never completely confidential, as it must be registered with the French tax authorities, while the *Registre National des Fiducies* shares key information of this agreement with, inter alia, the public prosecutor and law enforcement officers. This is a further reason for the *fiducie* agreement to be drafted with great care and caution.

3. Main advantages in case of insolvency proceedings of the debtor

As a preliminary remark, it has to be noted that the opening of insolvency proceedings against the trustee does not affect the trustee's estate created by the *fiducie*¹⁴. Nevertheless, assets included in this estate can be seized, but only by creditors in virtue of claims

arising from the possession or the management of such assets. In the event the trustee's estate is insufficient to satisfy all the creditors, they can seize the settlor's assets, except if provided otherwise in the *fiducie* agreement¹⁵.

In the event the debtor – who is usually the settlor – defaults under the agreement secured by the *fiducie*, the creditor(s) may permanently appropriate or instruct the trustee to enforce over the assets placed in the *fiducie* which, by virtue of this mechanism, are no longer owned by the debtor. As the insolvency proceedings only affect the debtor's assets, those placed in the *fiducie* are excluded from the insolvency proceedings and are out of the reach of the court appointed administrator/liquidator. However, the creditors' rights and protection will be affected depending on the nature and the different stages of each insolvency procedure as well as possession or not of the secured assets.

3.1. Safeguard (“procédure de sauvegarde”) and judicial reorganisation (“redressement judiciaire”) proceedings (the “Proceedings”)

- a) Existence of an agreement whereby the assets placed in *fiducie* remain in the settlor's possession - “*le constituant conserve l'usage ou la jouissance des biens transférés*”

In the event such an agreement (“*convention de mise à disposition rémunérée ou non*”) is entered into, article L. 622-23-1 of the French Commercial code provides that no transfer of the *fiducie* assets to the beneficiary(ies) or to a third party may be completed merely because of the opening of the Proceedings to the benefit of the settlor, the adoption of a reorganisation plan or a default prior to the opening of these Proceedings. Otherwise, the transfer is null and void.

Therefore, as long as the settlor complies with the safeguard plan or reorganisation plan, the beneficiary(ies) is/are not entitled to enforce over the trust assets included within the scope of the *fiducie* agreement or instruct the trustee to do so.

However, in case of breach and termination of the safeguard/reorganisation plan and the subsequent conversion of these procedures into a liquidation procedure, the security interest created

by the *fiducie* agreement becomes immediately enforceable and the relevant asset(s) can be transferred either to the creditor(s) or sold on arm's length basis.

- b) In the case where the settlor does not have possession over the assets transferred into the *fiducie* (“*dans l'hypothèse d'une dépossession du constituant des biens transférés dans le patrimoine fiduciaire*”)

In such case, the beneficiary(ies) may request the transfer of title of the assets to its/their benefit or the realisation of such assets, immediately upon the opening of a safeguard or judicial reorganisation proceedings.

- c) Ongoing contracts (“*contrats en cours*”)

The French Commercial code¹⁶ excludes the *fiducie* agreement from the agreements which may be terminated by a court appointed administrator. Therefore, the *fiducie* assets may not be returned to the debtor's estate due to the opening of the Proceedings and the termination of the *fiducie* agreement by the administrator.

However, the agreement placing the *fiducie* assets at the settlor's disposal (“*contrat de mise à disposition*”) may be subject to termination by a court appointed administrator. In such an event, the possession of the assets placed in the *fiducie* will be transferred back to the trustee, thus enabling the beneficiary(ies) to enforce its/their security.

- d) Creditors' committees

The creditors benefiting from the *fiducie* agreement cannot become members of the creditors' committees for the part of their debt which is secured under the *fiducie*¹⁷. As a consequence thereof, a debt waiver or a capitalisation of their debt may not be imposed for the portion of their debt secured under the *fiducie*.

3.2. Sale plan of the settlor's assets (“*plan de cession*”)¹⁸

In this situation, the *fiducie* assets will be excluded from the assets which can be transferred as part of a sale plan (“*plan de cession*”). Therefore, the beneficiary(ies) will not be impacted by the sale of the

debtor's assets. Contrary to other security rights where the preference right of the secured parties is exercised on the price paid by the purchaser (which is often below the market value of the assets), the position of the beneficiary of a *fiducie* is much more favourable.

Finally, in accordance with Article L. 642-7 of the French Commercial code, the "*contrat de mise à disposition*" (allowing the debtor to maintain use of the *fiducie* assets) may only be transferred by court order to the purchaser in the case of a sale plan if the beneficiary(ies) of the *fiducie* agree(s) to such transfer, giving the beneficiary(ies) another possibility to appropriate or enforce over the assets if he/they decide(s) against such transfer.

3.3. Liquidation proceedings

Enforcement of the *fiducie* is permitted from the opening of a court ordered liquidation procedure. The beneficiary(ies) is/are entitled to receive the full net proceeds of the sale of the *fiducie* assets without the other creditors of the insolvent debtor having a claim over such proceeds. This includes secured creditors and a "*convention de mise à disposition des biens au profit du constituant*" does not affect this right.

Lastly, creditors who wish to guarantee their claim through a *fiducie* must note that in the context of a liquidation proceeding, creditors can be held liable if the *fiducie* is deemed disproportionate to their claim (e.g., if the market value of the assets secured by the *fiducie* is/are much higher than the guaranteed claim)¹⁹. In such an event, the *fiducie* may be voided or reduced by a judge.

4. Tax regime

The *fiducie*, notwithstanding its advantage from a security perspective, has not been as successful as expected, mainly due to an unsuitable tax regime providing that the transfer of titles to the *fiducie* by the settlor was not covered by the *sociétés mères* tax regime²⁰ and the integration tax regime.

- The *sociétés mères* tax regime provides that if a company holds a minimum of 5% of another company's shares for at least two years, income arising from these shares will not be taxed

(notwithstanding a flat rate of 5% on such income)²¹.

- The integration regime provides that if a company holds more than 95% of one of its subsidiary's shares, it is allowed to consolidate its tax result with such a subsidiary²².

Prior to the 2014 tax reform, the debtor who contributed shares to the *fiducie* as security to its creditors could lose the benefit of these two regimes as such shares would not be applied in the determination of the above thresholds.

The 2014 Amending Budget law, applicable as from 31 December 2014, introduced new articles²³ in the French Tax code which provide that the shares contributed to a *fiducie* have to be taken into account for the determination of the threshold allowing the company which contributed shares to the *fiducie* to benefit from the *sociétés mères* tax regime and the integration regime.

In respect of the *sociétés mères* tax regime, the new regime also provides that the contribution of shares by the debtor to the *fiducie* does not interrupt the two year mandatory detention period.

In order for the debtor to benefit from these new provisions, the voting rights attached to the contributed shares must solely be exercised by the settlor, or by the trustee acting on the debtor's instructions.

Conclusion

Although the *fiducie* appears to be a very effective type of security interest for creditors²⁴, it has not met the expected success since its introduction into French law. The recent reform of the *fiducie*'s tax regime will certainly act as an incentive for debtors and lenders and eventually unveil the great potential of the *fiducie*.

1 The authors would like to thank Thomas Allain, trainee, and Kalish Mullen, associate, for their involvement in the preparation of this article.
2 Law n° 2007-211, 19 February 2007.
3 Article 2011 of the French Civil code (Code civil).
4 Law n° 2008-776, 4 August 2008; order n°2008-1345, 18 December 2008; order n° 2009-112, 30 January 2009; law n° 2009-526, 12 May 2009.

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- 5 Article 71 of the Law n° 2014-1655, 29 December 2014.
- 6 Law n° 2008-776, 4 August 2008, enforced as from 1 February 2009.
- 7 Article 2018 of the French Civil code (*Code civil*).
- 8 Article 2372-2 of the French Civil code (*Code civil*).
- 9 Article 1 of the decree n° 2010-219, 2 March 2010.
- 10 The “*période suspecte*” is the period comprised between the payment failure date and the opening judgment of the insolvency proceeding. The *fiducie* can be voided by the administrator if it has been entered into during this period (Article L. 632-1 9° of the French Commercial code).
- 11 Article 2026 of the French Civil code (*Code civil*).
- 12 Article 2027 of the French Civil code (*Code civil*).
- 13 “Procédures de sauvegarde ou de redressement judiciaire”.
- 14 Article 2024 of the French Civil code (*Code civil*).
- 15 Article 2025 of the French Civil code (*Code civil*).
- 16 Article L. 622-13 VI of the French Commercial code (*Code de commerce*).
- 17 Articles L. 626-30, L. 626-30-2 and L. 626-32 of the French Commercial code (*Code de commerce*).
- 18 This is the French equivalent to a sale of the business under section 363 of the Bankruptcy Code.
- 19 Article L. 650-1 of the French Commercial code (*Code de commerce*).
- 20 Parent-subsidiary regime, equivalent to tax consolidation.
- 21 Article 145 of the French Tax code (*Code général des impôts*).
- 22 Article 223 A of the French Tax code (*Code général des impôts*).
- 23 145 1-c §6 and 223-A §4.
- 24 This efficacy has led several prominent academics to present the *fiducie* as “*la reine des sûretés*”.

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