

AMERICAN BANKRUPTCY INSTITUTE JOURNAL

Issues and Information for Today's Busy Insolvency Professional

Making France a More Attractive Forum for Restructuring in Europe: Part I

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Editor's Note: In 2006, €7 billion of leveraged buyout (LBO) debt was granted in France with nearly €0 billion more added in 2008. According to sources, approximately a third of this debt was in default in 2008.¹ This article, appearing in two parts, examines the latest developments in France in the area of prepackaged restructuring plans—a new, attractive and innovative technique for distressed companies that looks set to be increasingly trialed and tested over the coming months to deal with the potential fallout from such default.

In the United Kingdom and the United States, prepackaged plans (pre-packs) have become standard practice in insolvency proceedings, where they are well-recognized as a practical tool. That said, both nations' approaches are not directly comparable in terms of process. In the U.K., a pre-pack is achieved by way of an administration proceeding, with the objective being to obtain a rapid sale of a distressed business to a predetermined buyer, with agreement being negotiated with the proposed administrators prior to any court process.

In the U.S., a chapter 11 proceeding is the preferred legal route and has more options. The usual approach, if there are minority dissenters, is to vote on an agreed-upon plan prior to commencing a chapter 11 proceeding. In this way, the required majority of creditors is able to impose their will on the minority—a key component of a chapter 11 pre-

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safeguards have been reinforced in the form of SIP 16,⁴ introduced in January 2009 to encourage greater transparency in cases where an insolvency practitioner envisages using a pre-pack solution.

In the U.S., pre-packs have become more commonplace as the surge in bankruptcies continues. In some cases, courts have issued guidelines for practitioners on pre-packaged chapter 11 proceedings.⁵

In France, the pre-pack does not have an equivalent history. It is a new concept for the bankruptcy courts, made possible only recently thanks to a 2005 law that

pack process.² The pre-pack is designed to allow a distressed business to be reorganized quickly. By design, a pre-pack arrangement removes or minimizes the delay and uncertainty in the insolvency process that might otherwise

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derail a turnaround arrangement. It also has cost advantages.



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Despite its attractions, a criticism not infrequently leveled at pre-packs is that the purchaser of the business may not be at arm's length (the purchaser may be a company owned by or related to the managers of the distressed business). While motive may be questioned on any given pre-pack arrangement, the countries in which pre-packs have evolved continue to explore its limits.

In the U.K., courts have not been hostile to the concept.³ Most recently,

was amended in 2008,⁶ but does not have the guidelines that exist in the U.K. and the U.S.⁷

The 2005 law introduced a new insolvency process that safeguarded proceedings and was inspired by the U.S. chapter 11 proceedings. The passage of the 2008 reforms has made safeguard proceedings more attractive to a debtor

⁴ A Statement of Insolvency Practice (SIP) constitutes guidelines to practitioners operating in an insolvency context, issued with a view to maintaining certain standards. SIP 16 was issued under procedures agreed upon among the insolvency regulatory authorities acting through the Joint Insolvency Committee (JIC). It was commissioned by the JIC, produced by the Association of Business Recovery Professionals, and has been approved by the JIC and adopted by a number of regulatory bodies in the United Kingdom.

⁵ See, for example, the U.S. Bankruptcy Court for the Southern District of New York.

⁶ The amended legislation came into force on Feb. 15, 2009.

⁷ It should be noted at the outset that what is now referred to as a "pre-pack" arrangement in France differs from the U.S. chapter 11 pre-pack equivalent in one key aspect: The operative voting takes place after commencement of the court process, not before. In this sense, the French "pre-pack" is more akin to a U.S.-styled prenegotiated plan. In common parlance, French practitioners nevertheless speak of a "pre-pack" arrangement—training on "pre-packs" was recently offered to French judges in July 2009. We therefore adopt the term "pre-pack" in this article.

¹ See Les Echos, April 24, 2009, p. 26.

² See *Bankruptcy in Practice*, published by ABI, 4th Ed 2007, p. 464.

³ See, e.g., *DKLL Solicitors v. Revenue and Customs Commissioners* (2008) 1 BCLC 112.

facing financial difficulties. French courts are only beginning to see the emergence of pre-pack techniques, with debtors negotiating turnaround arrangements with major creditors, and then invoking safeguard proceedings to carry the arrangement through and bind other creditors. For the first time in France, there is now a real prospect of a significant degree of “contractualised” restructuring organised through a court process.

Safeguard Proceedings

Safeguard proceedings represent one of five types of proceedings currently available in France to a financially-distressed debtor.⁸ While not expressly interlinked, the different types of proceedings may complement one another, with one proceeding capable of following another as necessary. Whereas agreement of main creditors may not be enough to turn around the distressed debtor under available preventive proceedings,⁹ it may be sufficient in safeguard proceedings to bind the minority to a restructuring plan proposed by a majority creditor or the debtor’s management.

The 2005 law that introduced safeguard proceedings came into force on Jan. 1, 2006, and received an almost immediate baptism of fire when Eurotunnel filed for safeguard proceedings to restructure its considerable debt in July 2006. Although it took a year before a restructuring plan surfaced from the proceedings, the result has generally been considered a success. In February 2009, some 22 years after its incorporation and nearly 15 years since it started operations, Eurotunnel announced its first-ever dividend to shareholders.¹⁰

Safeguard proceedings have all the characteristics of a collective insolvency

procedure¹¹ but differ from judicial reorganisation and liquidation proceedings in that they can only be invoked prior to the debtor encountering cashflow problems, at which time safeguard proceedings are no longer an option.¹²

The central feature of safeguard proceedings, as opposed to judicial reorganisation or liquidation proceedings, is that the debtor remains largely in control of the business.¹³ The 2008 reform significantly reinforced this aspect: The debtor is now permitted to propose his or her chosen administrator, the debtor draws up the restructuring plan (previously the duty of the administrator), and it can no longer be a condition of the restructuring plan that management be removed. Under the new law, while the court will appoint an administrator to accompany management in the safeguard process, the administrator’s role will be limited to that of an informed observer and guide.

When given the task of simply overseeing the company, the administrator’s assignment consists, first and foremost, in checking that the management’s actions are not compromising creditors or the company’s recovery. If given the responsibility of supporting management, the administrator’s primary role is to countersign management decisions made by the distressed company’s directors. While the administrator continues to play an important role, since the 2008 reform, the administrator cannot supplant management in the context of safeguard proceedings.

Another significant feature of safeguard proceedings is the automatic stay of claims that arises upon commencement of the proceedings. This protection provides the backdrop against which the debtor will seek to reorganise its affairs.

Finally, particularly in the context of a pre-pack arrangement, the role of the creditors’ committees is important. In any significant safeguard proceedings, the debtor is required to put its restructuring plan to the vote of two creditors’ committees. The first committee is made up of financial and assimilated institutions, while the second is made up of the debtor’s principal suppliers. Since the 2008 reform, a third body of stakeholders must also approve the plan—the bondholders (if any). In all cases, decisions are taken

in each committee by majority vote comprising two thirds of the total amount of claims made by the members who vote.

Where the creditors’ committees approve a safeguard plan, the plan is not subject to a number of restrictions that would otherwise apply.¹⁴ For example, the plan may extend beyond 10 years and there is no requirement that the first repayments be made within a year, or that repayments equal at least 5 percent of the total due for each subsequent year. As well, creditors may be treated differently provided it is justified by the situation, and in the case of a company limited by shares, debt may be exchanged for equity.

Those creditors who are not members of a creditors’ committee must be consulted individually or collectively.¹⁵ Unlike their committee counterparts, no reduction in their claims may be imposed, and this is the case irrespective of whether a safeguard plan is voted through by the creditors’ committees. Indeed, it is not possible to impose on noncommittee creditors any of the more flexible arrangements (described above) that can be included in a plan that is voted through by the creditors’ committees. In this respect, there may be an advantage in not being on a creditors’ committee. At the end of the process, the restructuring plan is approved by the court, which then appoints a commissioner to oversee implementation of the plan.

Pre-pack à la Française

The new law provides a workable structure within which to operate a pre-pack arrangement. While it is not possible to simply have the court approve a preagreed restructuring plan with no voting by creditors in the court process, if a sufficient number of creditors are willing, a restructuring plan can be put in place.¹⁶ One clear limitation is that any restructuring plan proposed by the debtor needs the support of at least two, and possibly three, classes of creditors before it will be capable of expedited pre-pack treatment. Where bondholders exist, as is not infrequently the case for companies of a certain size, and almost invariably for LBOs, priority lenders will not necessarily be able to impose the plan over recalcitrant junior lenders, even if the priority lenders are unanimous in their view. Reductions in debt cannot be imposed on creditors who are not members

⁸ In addition to safeguard proceedings (*procédure de sauvegarde*), the other four types of proceedings are (1) ad hoc representative (*mandataire ad hoc*), a type of mediator to whom resort in practice is not infrequently made and whose role was fully recognized in the 2005 law; (2) conciliation (*conciliation*), introduced in the 2005 law, replacing the former composition with creditors procedure; (3) judicial reorganization (*redressement judiciaire*); and (4) judicial liquidation (*liquidation judiciaire*). Ad hoc representative and conciliation proceedings are commonly referred to as “preventive” procedures.

⁹ See fn. 8.

¹⁰ Litigation surrounding the Eurotunnel safeguard proceedings continues nevertheless. In particular, the gambit of third-party proceedings directed at the commencement order are still going through the courts. In a series of decisions handed down on June 30, 2009, the French Supreme Court overturned the Paris Court of Appeal in connection with third-party applications to review the commencement orders affecting Eurotunnel PLC, Eurotunnel Finance Ltd., Eurotunnel Services Ltd. and Eurotunnel Plus Ltd.—all companies incorporated in the U.K. In the court of appeal, the third-party applications to review were dismissed on the grounds that a third-party creditor, at a threshold level, had to show fraud or a distinct interest (*motif propre*) in order to challenge a commencement order authorizing safeguard proceedings. The French Supreme Court has referred the matter back to a reconstituted Paris Court of Appeal for reconsideration. The substantive issue turns on the application of article 3 of EU Regulation 1346/2000 and whether the French courts have jurisdiction to commence safeguard proceedings affecting each of the Eurotunnel companies, which depends on determining the centre of main interest (COMI) of each debtor company. Under article 3, the place of the registered office (*i.e.*, the U.K. in this case) is presumed to be company’s COMI, subject to contrary proof.

¹¹ Safeguard proceedings are expressly recognized as collective insolvency proceedings under EU Insolvency Regulation 1346/2000, Annex A.

¹² In French terms, the critical criterion is that of payment failure (*cessation de paiements*) where the debtor is no longer able to meet current debts from available assets.

¹³ Safeguard proceedings nevertheless remain subject to overarching control by a court-appointed supervisory judge and, ultimately, the Court itself.

¹⁴ Refer to Commercial Code L.626-30-2, para 2.

¹⁵ All credit institutions or similar, and all major suppliers, are members of a creditors’ committee as of right. See fn. 17.

¹⁶ This situation may be contrasted with the possibilities offered by chapter 11 proceedings. Under U.S. law, there is a specific chapter 11 provision that precommencement acceptance by a creditor constitutes acceptance of the restructuring plan on its part, without the requirement of any further vote in the court process, provided that the creditor in question received proper disclosure. See 11 U.S.C. §1126(b). No such provision exists under French law.

of a creditors' committee.¹⁷ However, it is possible to sell off or assign parts of the debtor's activity as an adjunct to any safeguard plan,¹⁸ but the debtor may elect to sell or assign particular assets.¹⁹ At the end of the process, the court remains final arbiter on whether a plan is approved and is required to ensure that "the interests of all creditors are sufficiently protected."²⁰ The committee-voting process does not offer carte blanche to the debtor, who has the support of the majority of creditors to freely rewrite the debtor's future.

In terms of speed of execution, which is a critical feature of any pre-pack arrangement, the new law provides a challenging environment. Within any safeguard proceedings, there are a number of time limits that, on first appearance, would appear to make a speedy resolution impossible to achieve, not least of which being the time within which proofs of debt must be lodged (two months for creditors situated in France, four months for overseas creditors).²¹ Other limits include: the time within which committees must vote on the restructuring plan (20-30 days);²² a limitation on convening bondholders only after the creditors' committees have voted (15 days notice);²³ and the time within which creditors outside of the committees must respond to proposals on accommodating their claims (30 days).²⁴ Despite this, it is possible with careful planning, cooperation from stakeholders and diligence to obtain a court-approved restructuring plan within 60 days from the date of commencement of the safeguard proceedings.

Prior to commencing the safeguard proceedings, the full four- to five-month

statutory period of conciliation, or most of it, will undoubtedly be needed to enable negotiation with the stakeholders and proper preparation to ensure expeditious treatment in the safeguard proceedings. Speed and security is assisted by the fact that the court is required to rule on any challenges to the composition of the committees, any procedural irregularities and the content of the plan, at the same time as it rules on whether to adopt the plan.²⁵ It is noteworthy as well that in the case of a plan that stays on track for more than two years, after which the debtor can request that any trace of the procedure and plan be expunged from the company's register.²⁶

In Part II, we will look at the practical application of the French pre-pack approach to cases currently or recently before the courts. ■

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¹⁷ From amongst suppliers, those whose claims represent more than 3 percent of total claims are members of the suppliers' committee as of right. Commercial Code L.626-30 and R.626-56. The administrator has the power to invite other nonqualifying suppliers to become a member of the committee (R.626-57). See fn. 24.

¹⁸ Commercial Code L.626-1. The part to be sold or assigned must constitute "a group of means of production that form one or more complete and autonomous branch or branches of activity" (L.642-1). Any such sale/assignment will be subject to the same restraints as would apply in the case of a sale or assignment in liquidation, including as to publicity (L.642-22). In the context of safeguard proceedings, one complication is that it is not possible to simply agree an assignment or sale between the debtor and the intended purchaser. The process requires that offers be invited and approved by the Court. As part of the safeguard proceedings commencement order, it would be prudent to seek a short time limit within which offers should be tendered so as to minimize the possibility of any disruption to pre-pack arrangements (refer to L.642-2).

¹⁹ In this case, the proceeds would revert to the debtor, subject to any liens or security interests (Commercial Code L.626-23).

²⁰ Commercial Code L.626-31.

²¹ Time runs from publication of the safeguard proceedings in the Official Bulletin of Civil and Commercial Announcements (BODACC).

²² This period may be reduced to 15 days by the supervising judge upon application of the debtor or administrator; Commercial Code L.626-30-2, para 3. Bondholders may only vote after the plan has been accepted by the creditors' committees.

²³ Commercial Code R.626-60.

²⁴ In practice, the administrator will send out proposals for a reduction in claims and/or extension of time for payments. Failure by the creditor to respond within 30 days of receipt of the administrator's letter is deemed to be acceptance of the proposal (Commercial Code L.626-5). However, the creditor can refuse the proposal, in which event no reduction of the creditor's claim can be imposed in the safeguard proceedings.

²⁵ Commercial Code L.626-34-1. Commentators have referred to this conjuncture as a mechanism to "purge" claims from the outset of the plan that might otherwise be brought by disgruntled creditors to disrupt the legal process and thwart efforts of the majority creditors/the debtor.

²⁶ Commercial Code R.626-20. Introduced with the 2008 reforms, this is clearly an attractive provision for the debtor but may obscure matters for new partners who are introduced to the debtor after the two-year window has expired.

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In 2006, €67 billion of leveraged buyout (LBO) debt was granted in France with nearly €20 billion more added in 2008. According to certain sources, approximately a third of this debt was in default in 2008.¹ This two-part article examines the latest developments in France in the area of pre-packaged restructuring plans—a new, attractive and innovative technique for companies in difficulty that looks set to be increasingly trialed and tested over the coming months to deal with the potential fallout from such default.



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In Part I, we examined the novelty of the pre-pack for French practitioners, outlined its main features in the context of French safeguard proceedings and made some comparisons with the pre-pack approach in the context of U.S. chapter 11 proceedings. In Part II, we comment on a recent significant example of the pre-pack à la française in action.

Pre-pack a la Française: The Autodis Example

The first significant, practical application of the pre-pack possibilities offered by the 2005 safeguard proceedings, as amended by the 2008

¹ See Les Echos, April 24, 2009, p. 26.

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order, is illustrated by the case known as *Autodis*, a holding company in significant financial difficulties, controlled by a private equity investor.² The result was a positive one for *Autodis*.

Through the safe-guard and related procedures, the *Autodis* Group managed to reduce its debt by almost €600 million

group, with the new investor obtaining a controlling interest. New finance in the order of €34 million was obtained from two other lenders and secured through the conciliation process.³ Last, under the restructuring plans presented by *Autodis* and *Parts Holdings* (France), no redundancies were forecast, this being a significant element to the plans in a country known for social unrest when it comes to layoffs.



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Immediately after the coming into force of the 2008 reform, applications for safeguard proceedings were filed in respect of *Autodis* and *Parts Holdings*. On Feb. 18, 2009,

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with lenders being given the option of equity or taking up bond arrangements within the group. *Autodis* was able to shed 70 percent of its priority debt, 100 percent of secondary debt and 100 percent of its repayment obligations under bonds. Under the restructuring plan, suppliers and other creditors were required to be paid in full within two months of adopting the plan.

A new investor joined the majority shareholder, and together they injected almost €110 million in new capital and cash via convertible bonds into the

the court ordered commencement of safeguard proceedings with respect to both companies. In tandem with the safeguard proceedings, *Autodistribution* undertook negotiations with its principal stakeholders under the umbrella of the confidential preventive procedures contained in the 2005 law.⁴ On April 6, 2009, the court approved the restructuring plan proposed by management in the safeguard proceedings, as well as the agreement reached in the conciliation proceedings.

The safeguard proceedings were necessary to allow the company to impose the restructuring plan on a minority of *Autodis*' banking partners

² While the case is referred to as *Autodis*, it also concerned *Parts Holdings* (France) and *Autodis* operational companies, including *Autodistribution*, employing in excess of 6,000 employees. Together, they form the *Autodistribution* Group of companies—a group specializing in the supply of car parts. Over the last 10 years, the *Autodistribution* Group has been through various restructurings involving a number of well-known private-equity interests. It is perhaps not surprising that it should be the first notable entity to test the 2008 reforms.

³ See fn. 8.

⁴ Principally conciliation proceedings. The court appointed a conciliator on Feb. 9, 2009.

who would not agree to it.⁵ Using the safeguard proceedings, Autodis was able to “cram down” uncooperative creditors. A qualified majority vote in the creditors’ committees was sufficient to carry through the debtor’s proposals.⁶

The parallel conciliation process undertaken alongside the safeguard proceedings allowed the stakeholders to have time, on a confidential basis, to explore the options in relation to Autodistribution.⁷ Court approval of the agreement reached at the end of the conciliation process was essential to ensure that the “new money” loaned to Autodistribution by the financial institutions would enjoy the special priority accorded under the new law.⁸ As a result, once agreement was reached with the necessary number of creditors, it took less than two months to achieve court approval of the overall restructuring plan.⁹

Conclusion

While the French system has undoubtedly shown itself to be more flexible than in the past, some notable barriers remain to a wholesale adoption of the pre-pack approach, not the least of which is the attitude of the various participants in the insolvency process, who are steeped in the previous practice of insolvency law and procedure. As previously noted herein, safeguard proceedings are only available where the debtor is not in a payment-failure situation—in other words, at the time of filing, a debtor must be capable of meeting its current liabilities out of its disposable assets.

Furthermore, it should be noted that as a percentage of total insolvency procedures, safeguard proceedings remain relatively insignificant. Safeguard proceedings are on the rise but still only account for something in the order of 2

percent of the total number of collective insolvency proceedings in France.¹⁰ The number of safeguard proceedings involving a pre-pack arrangement will be smaller still, so that pre-packs are likely to affect mostly large companies and other significant companies subject to LBOs.

With that caveat, it is fair to say that *Autodis* has paved the way for future pre-pack arrangements *à la française*. While the French process may not be quite as flexible as U.S. chapter 11, the essential elements exist in French law to facilitate a speedy and effective turnaround arrangement. Undoubtedly, the law will gradually evolve to cater to practical issues that may arise as practitioners resort increasingly to the pre-pack process. Safeguard proceedings allow an embattled business to survive intact. Initially viewed by creditors with some suspicion as an escape route or unwelcome strategic tool for companies in difficulty, creditors and debtors alike are beginning to view matters differently and to seize the opportunities offered by the new process.

This is especially the case in light of the 2008 reforms. The arrival on the French scene of pre-pack arrangements is evidence of this changing attitude toward insolvency procedure. As well, there has been a notable change in the approach of French banks that now appear ready to take up equity for debt in the restructuring process. This is a previously unheralded development that presents new challenges for all stakeholders in distressed France-based companies.

French safeguard proceedings are also increasingly being used to benefit foreign companies in a company group situation. Thus, in the context of EU Insolvency Regulation (1346/2000), where it can be shown that the centre of main interest is in France, foreign subsidiaries or holding companies are able to give effect to cross-border restructuring in a centralised and coordinated fashion.¹¹ As a result, France now presents an attractive venue to those in management for whom forum-shopping may be a relevant issue.

Given the amounts of money injected into LBOs over the last few years, the number of occasions to further test the 2008 reform, as well as bank attitudes, is likely to multiply over the coming months. The prospect of a spate of future restructurings looks increasingly likely.¹² Those adept practitioners with a firm grasp of the commercial issues at stake, and pragmatic knowledge of the new statutory framework, should be kept busy. ■

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⁵ Of the members of the suppliers’ committee who voted, all voted in favour of the restructuring plan, as did the bondholders. However, the banks were not unanimous: Only 78.5 percent of the votes expressed by the banks were in favor of the plan.

⁶ Prior to the 2008 reform, voting in the creditors’ committees required a double majority: a majority in terms of number of creditors (whether they had voted) representing at least two-thirds of all claims represented by the committee. Since Feb. 15, 2009, with respect to voting rights, the December 2008 order removed the requirement of voting by a show of hands, and decisions are taken in each committee by majority vote comprising two-thirds of the total amount of claims made represented by the voting members. Commercial Code L.626-30-2. This change has served to concentrate voting rights into fewer hands and counters the risk of manipulation of the vote by subdividing claims.

⁷ The conciliator for Autodistribution was court-appointed on Feb. 9, 2009.

⁸ Provided the agreement reached through the conciliation process is court-approved, the lenders’ claims in any subsequent insolvency process will rank above all other claims, with the exception of limited wage claims enjoying “super priority” and certain court costs associated with the insolvency process. Commercial Code L.611-11. This aspect was an innovation of the 2005 law to encourage suppliers and banks to lend to and carry on business with companies in difficulty.

⁹ In the proceedings, the creditors’ representative noted that the time limit for lodging claims had not expired by the time the court approved the restructuring plan. This did not prevent the court from approving the plan, no doubt because the plan provided for payment in full of all suppliers within a relatively short time period.

¹⁰ The rise is nevertheless significant. Over the first nine months of 2009, 1,049 safeguard proceedings were commenced—up 137 percent on the same period in 2008 (source: Altares).

¹¹ Recent examples of this type of approach are offered by Société Heart of Défense SAS (French) and its holding company Dame Luxembourg SARL (Luxembourg), and Belvedere SA and its subsidiaries (six of which were Polish companies). Different countries have approached the critical notion of “centre of main interests” in different ways. The European Court of Justice (ECJ) has had occasion to rule on the matter in a battle for jurisdiction between the Irish and Italian courts in the Parmalat affair (Eurofood IFSC Ltd., ECJ Case, C-341/04, Judgment of the court (Grand Chamber), May 2, 2006). The notion of “centre of main interests” is at the heart of the ongoing challenges to the Eurotunnel proceedings.

¹² Apart from Autodis, other recent known examples of LBOs in difficulty, such as Desjonquères, Sia, Matéris, Monier and Terreal, may be only the tip of the iceberg.