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How to deal with insolvency of distributors/franchisees

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IMPACT OF THE DISTRIBUTOR'S BANKRUPTCY IN BELGIUM

Introduction

In Belgium the matter of bankruptcy is regulated by the Law of 8th August 1997, which became effective on the 1th January 1998, and has been modified several times over the last years.

This law settles the conditions and development of the bankruptcy procedure, including its consequences. The provisions of this law can substantially also be applied to the specific case of distributor bankruptcy.

In case of bankruptcy of the distributor, which transactions with the supplier can be revoked?

According to the above-mentioned law in the case of bankruptcy, different transactions, acts and payments must or can be considered unenforceable towards the creditors of the distributor.

Firstly, obviously, all acts or payments made by the distributor or to him after the declaration of his bankruptcy (art. 16 of the Law) are unenforceable.

Secondly, the following transactions are by full right also unenforceable, in the case they are made by the distributor during the "suspect period" i.e. during the period between insolvency and the declaration of bankruptcy, which may not be more than 6 months before the bankruptcy (art. 12 and 17 of the Law):

- free transactions concerning movable and immovable goods or damaging contracts which are characterized by the disproportion of mutual obligations;

- payments for debts not yet expired or payments for debts expired but made in a different manner than the one established. In this respect, for example, the termination of a sale during the "suspect period" is theoretically enforceable to the creditors, but the return of the goods could also conceal a different manner of paying the debts.

- the securities acted on the goods of the distributor for previous debts.

As far as these two hypotheses are concerned, whenever the conditions are met, the Court must declare the transaction unenforceable, without possibility of having a choice.

On the other hand, all payments not provided for in art. 17 and made during the "suspect period", may be declared unenforceable (but do not necessarily have to be), if the party that has contracted with the distributor was aware of his insolvency (art. 18 of the Law). In this case the curator is not obliged to claim the unenforceability, but is entitled to evaluate the opportunity of such a claim.

Indeed, in this respect three conditions are to be met: the transaction has to take place during the "suspect period", the curator has to prove that the counterparty was aware of the insolvency and the payment must have caused a serious damage for the other's creditors.

Furthermore, independent of the date when they are made, all the acts and payments in fraud for the creditors are unenforceable (art. 20 of the Law). In this respect the curator has to prove the fraud of the debtor and the damage for the creditors.
Finally, according to art. 19 of the Law, the inscription of securities after the insolvency of the debtor can be declared unenforceable when, between the date of the act of securities and the date of his inscription, more than 15 days elapsed. Also the curator may take action in the case of payment of a bill of exchange during the "suspect period" (art. 21 of the Law).

Once the unenforceability is declared, the party that has contracted with the distributor, must return the goods to the curator or, if the goods cannot be returned, their value or, in case of payment, the amounts received and may also be condemned to pay interest. The curator and the creditors are entitled to not take into account the transaction made with this party.

Is it possible to terminate the contract and to appoint another distributor once bankruptcy has been declared?

The issue concerning the continuation or the termination of ongoing agreements after the bankruptcy declaration is regulated by art. 46 of the Law.

According to this disposition, theoretically the contracts concluded before the bankruptcy are not automatically terminated because of that. Indeed it is one of the tasks of the curator to decide whether is preferable for the creditors to continue the pending agreements or not. The other party of the contract can notify the curator to take a decision within 15 days. In case of no decision by the curator, the agreement is considered terminated by full right and the other party is entitled to claim damages and interests, if any, for the termination. These damages will be considered as a debt "dans la masse". On the other hand, in case of continuation of the agreement by the curator, the other party is entitled to claim the execution of the obligations of the agreement and, in default, can invoke the *exceptio non adimpleti contractus* or the right of retention.

However it must be pointed out that in the case of contracts characterized by the *intuitu personae*, the bankruptcy involves automatic termination of the agreement. As concerns the distribution agreement, it must be established whether the contract could or not be considered as *intuitu personae*.

This character has to be proved and depends on the circumstances of each contract. In the case of the affirmative, once the bankruptcy of the distributor is declared, the supplier can inform the distributor of his intention to terminate the agreement and is entitled to appoint another distributor. In the negative case, the above-mentioned rules will be applicable.

Furthermore the contract can also be considered as terminated whenever a resolution clause is inserted in case of bankruptcy. This kind of clause is valid, but the other party to the contract has to invoke its application in order to terminate the agreement.

Is it possible to recover goods in the possession of the distributor if there has been retention of title?

In case of bankruptcy of the distributor, the following conditions must be fulfilled so that the reservation of title will be effective and opposable towards third parties (art. 101 of the Law):

(i) the clause must be settled in writing and both parties must have agreed, eventually also tacitly, at the latest upon delivery of the goods. In the case that this clause would be inserted in the general conditions of sale or in a framework agreement, the reservation of title will be applicable to various deliveries, without the need for a singular acceptance for each sale,

(ii) the goods have to be in kind with the distributor and must remain movable. This means that if the distributor should no longer be in possession of the goods, the disposition of art. 2279 of the Belgian Civil Code will be applied. According to this article, the third party being a *bona fide* purchaser shall be protected. In addition, according to art. 2268 of the Belgian Civil Code, good faith is presumed. Only in case the third party had knowledge of the reservation of title or, in his capacity as a merchant should have been aware of the existence of the reservation, this party will not be able to appeal to article 2279 of the Belgian Civil Code. Otherwise, the supplier will not be entitled to claim the *reivindicatio* of the goods; in other words, the reservation of title is not transmissible and the seller is not entitled to claim from the purchaser;

(iii) the *reivindicatio* must be claimed before the end of the examination of all claims.

However, it should be stressed that in case the *reivindicatio* is claimed from the supplier, the curator has the possibility to avoid the recovery of the goods by paying the amount agreed between the supplier and the distributor, excluding interest and penalties.

Finally it needs to be considered that whenever the curator has sold the goods, which are the object of the reservation of title, without being aware of the right of property of the supplier, the latter will only be entitled to receive the price paid.

Can the supplier be held responsible towards the distributor's creditors if he has continued supplying, notwithstanding the insolvency?

In respect of this question, it should be underlined that is rather strange and exceptional that the supplier continues supplying, despite being aware of the insolvency of the distributor.
In such a situation, there is no reason nor is it in his interest for the supplier to continue with the contract and indeed we have never incurred a similar case.

However in this respect, it frequently happens that the bank or the credit institutions are held responsible towards the creditors for inappropriately granting credit, which worsens the situation of the bankrupt party and contributes to the bankruptcy. We may consider that such a liability can also be claimed from a supplier who has contributed to hiding the insolvency of the distributor and to creating an appearance of a positive financial situation.
Despite that, in this case it needs to be proved that the supplier was aware of the insolvency, that in a similar situation a prudent and good trader should not have continued supplying and that such behaviour has caused damage to the distributor's creditors.

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