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Management fee agreements can be nullified for lack of cause

In a judgment dated July 4, 2013[1] the Paris Court of Appeals has recalled that a management and services agreement entered into between a provider and a beneficiary is void wherever this agreement overlaps with the exercise of a corporate management mandate within the beneficiary.

The facts of the case are as follows:

On June 27, 2007, a French *société par actions simplifiée* (simplified joint-stock company, or hereinafter "SAS") entered into an "*assistance, management and services*" agreement with a French *entreprise unipersonnelle à responsabilité limitée* (single-member limited liability company, or hereinafter "EURL") managed by one of the shareholders of the SAS, i.e. M.B.. Shortly thereafter, M.B. was appointed as general manager of the SAS.

Two years later, M.B. was removed from his position as general manager of the SAS and the agreement was terminated without notice and indemnity.

On August 10, 2009, the SAS was summoned before the Paris Commercial Court. In a judgment dated February 25, 2011, the Paris Commercial Court ordered the SAS to pay the sum of 98,567.68 € as termination indemnity.

On April 1, 2011, the SAS lodged an appeal against this judgment. On July 4, 2013, the Paris Court of Appeals, pointing out that some of the tasks provided for under the agreement corresponded in fact to functions that are customarily performed by the general manager of a company, held that the agreement was invalid, as per Article 1131 of the French Civil Code[2].

The Court grounded its decision on the fact that the **cause**[3] of this agreement, i.e. to have the SAS benefit from M.B.'s services, was **nonexistent** because the latter was supposed to provide the **same services in the framework of his mandate as general manager**.

This judgment is fully in line with a case-law trend that started in 2010[4] and that challenged many management and services agreements commonly referred to as "*management fee agreements*".

It points out that these agreements – the primary purpose of which is to reduce the operating costs of companies that are members of the same group by centralizing their so-called "support" functions – must, just like any other agreements, **have a cause**[5]. If it does not have a cause, the agreement is invalid and the provider can be ordered to refund the amounts it has unduly received.

If we strictly follow the definition given by Mr. G. Cornu, to be valid, the management fee agreement must be of interest to each of the contracting parties[6].

As such, it becomes obvious that an agreement, the purpose of which would be the performance by a provider to the benefit of a beneficiary of tasks customarily entrusted to the manager of such beneficiary, would be of no interest to the latter and, therefore, would be deemed without cause.

It is because of this basic principle that a specific attention should be paid to the nature of the services provided for under a management fee agreement, especially when the provider and the beneficiary are managed by the same person.

Any and all **services likely to overlap with corporate management duties** (e.g. definition of the strategy, management and representation) must be excluded from management fee agreements and replaced by specific services that are distinct from corporate management duties, e.g. provision of a financial, administrative, commercial or technical assistance.

The delimitation of the scope of the services must also be assessed on the basis of the activities carried out by the beneficiary as Courts may consider that certain services are in fact the responsibility of the manager.

Lastly, in addition to the risk of nullification discussed above, potential tax and criminal[7] implications should also be taken into account.

In a scenario – quite common in practice – where the **beneficiary** is a **SAS**, one option could be to avoid a management fee agreement, the future of which is now uncertain, and to appoint the provider as **President** of the beneficiary and pay it a (reasonable) compensation for the performance of its corporate mandate.

[1] Paris Court of Appeals, July 4, 2013, n°11/06318.

[2] "*An obligation without cause or one based on a false or an illicit cause cannot have any* effect".

[3] Under French contract law, four requisites are essential for the validity of an agreement: consent, capacity, a definite purpose which forms the subject-matter of the agreement and a lawful cause in the obligation.

[4] Cf. in particular: decision of the Commercial Chamber of the *Cour de Cassation* (French Supreme Court) dated September 14, 2010, n°09-16.084 and decision of the Commercial Chamber of the *Cour de Cassation* dated October 23, 2012 n°11.23.376.

[5] Cf. footnote 2 above.

[6] G. Cornu, *Legal terminology*: the cause is the "*interest that the legal instrument has for its author*".

[7] In certain cases, the contractual parties were prosecuted for mismanagement act and misappropriation of corporate assets.