# New Bill on Insolvency Code in Romania

## Simona Maria Milos writes on the financing of pre-insolvency and the codification of the insolvency law in Romania

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**In Romania, the Bill on insolvency code is ongoing to be legally approved – a normative act consisting of nearly all legal provisions in national and international insolvency and pre-insolvency matters.**

The shortcomings of the current regulation on the insolvency proceeding, consisting of Law no. 85/2006, signals from the business environment related to the inconsistencies of the normative framework, have grounded the decision of the Ministry of Justice of triggering an enterprising project to improve and put in a code frame of insolvency and pre-insolvency legal provisions.

Being an integral part of the Program regarding the judicial system reform (financed by a loan from the World Bank) the Bill on insolvency code enjoys of a technical assistance granted by a consortium having legal, practical and academic expertise, namely PWC SPRL (Romania), Stanescu, Milos, Dumitru & Associates Law Office, D&B David & Baias Law Office and the West University of Timisoara.

The first goal of the said project is to balance the interests of the most significant players acting in the insolvency proceedings – the debtor and its creditors, with regard to the possibility of having access to such proceedings, hindering the debtor of taking advantage, much too easily, of benefits of such a proceeding, to the detriment of its creditors.

Basically, the most important shortcomings of the Law no. 85/2006 which determined a broad amendment of the insolvency legislation and justified, until a certain point, the decision of the Government, is in a nutshell, the following:

- Prospect to confirm a reorganisation plan able to stipulate the payment of an insignificant percentage of the entire creditors' table, yet, being legally grounded. Such an action was made possible because the plan could have been approved following a sole condition, namely, half plus one of those – maximum – five claim classes meant to approve the plan, classes which could consist of, in terms of percentage, a tiny amount of all claims;
- Notwithstanding, the law makes mandatory the payment of current debts, born after the opening of insolvency proceedings, no sanction for breaching such an obligation being provided for the respective debtor.

However, the insolvency code had to set such unfairness in a manner able to allow an honest debtor to have access to actual and effective reorganisation proceedings.

It seems the authorities, intending to suppress abusive manipulative actions of *mala fide* debtors, reached, nearly in an ailing way, the very legitimate interest of those who, acting in a *bona fide* manner, want to run a reorganisation process, within a troublesome economy, severely undergoing the financial crises of previous years.

Thus, after having delivered the Bill on insolvency code, the Romanian Government has brought some major amendments with a significant impact on the insolvency proceedings.

With regard to the proposals brought by the Government, we shall refer hereunder only to three of the most significant amendments, namely:

1. Reducing the duration of the reorganisation plan from three years (duration already proposed) to only one year;
2. Setting of a percentage for confirming the reorganisation plan at 50% of total claims enjoying voting rights; and
3. Inserting the express possibility of foreclosure proceedings outside the insolvency proceedings, in favour of current claim owners, (Art. 75 (4) of the normative act bill).

Paradoxically, instead of reaching its purpose of harmonising the interests of the debtor and creditors involved in the proceedings, the new insolvency Code puts to an acid test any reorganisation strategy of an honest debtor.

With regard to the provisions, related to the short period of time of achieving the reorganisation plan and increment of the confirmation percentage to 50% of total claims, the core obstacle is represented by the fact that the most significant financing source of the reorganisation plan is the sale of assets and those depend on the investors' interest, which is very low at this time; on the other hand, it is quite impossible for the debtor to achieve an operational profit within one year, able to cover the payment of historical debts.

The authorities' argument in favour of the reduction of the plan duration was necessary because insolvency proceedings

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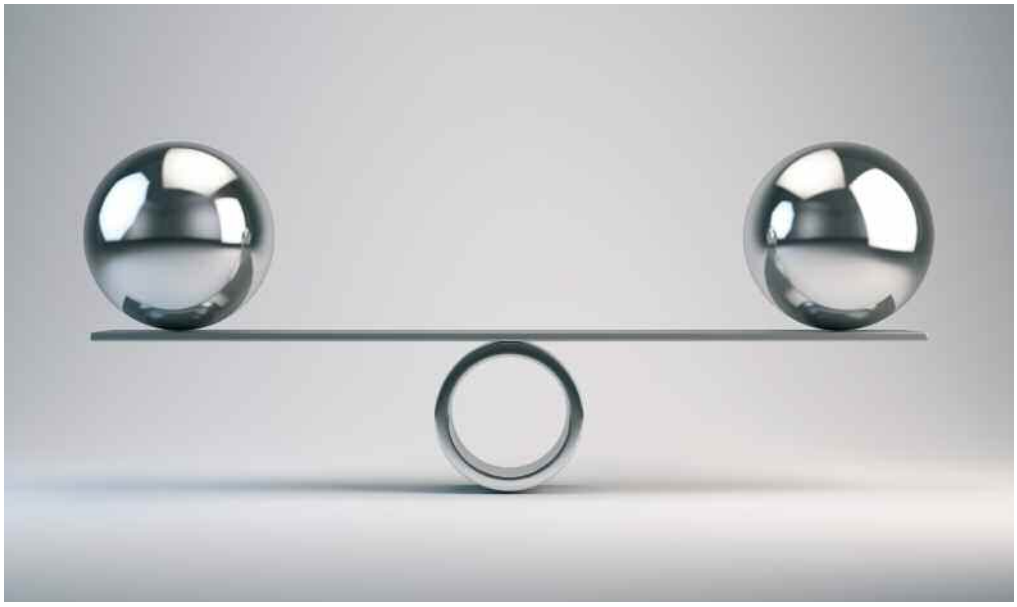

> THE FIRST GOAL OF THE PROJECT IS TO BALANCE THE INTERESTS OF THE MOST SIGNIFICANT PLAYERS ACTING IN THE INSOLVENCY PROCEEDINGS – THE DEBTOR AND ITS CREDITORS

lasting too long is not justified, insofar that it is not the duration of the plan itself or the problem of extending the proceedings, but the too long duration of the observation period.

Considering the atypical situations existing under Law no. 85/2006 where reorganisation plans have been confirmed following the vote of claim-holders owning insignificant percentages of the entire creditors' table, it became obvious and is rational to think of the necessity of taking into account a significant percentage of the entire liabilities.

Notwithstanding, the ceiling of 50% of the entire creditors' table, given the proposed 30% of total liabilities, could become excessive, leading to dominant positions of some creditors.

Briefly, we shall present further on the remedies already implemented in the insolvency Code, proving that the insertion of additional provisions was not necessary, damaging some fundamental principles of insolvency:

- with regard to current creditors, the insolvency Code reinstates their right to ask for the opening of bankruptcy proceedings of the debtor, should the latter fail to pay the claims within 30 days from the maturity date.
- with regard to the too easy approval of a reorganisation plan, the Code proposes a supplementary condition – the plan should be approved if a majority is reached by 30% of the total claim value.

All aforesaid actions, already adopted by the insolvency Code, prove there is no longer a way of justifying the granting of permission for implementing the debtor's foreclosure by the owners of current claims outside the proceedings, this opposing to any principles governing bankruptcy proceedings.

The rule in bankruptcy proceedings is the debtor's patrimony is subject to realisation within the same execution proceedings, considering all creditors must receive a *bankruptcy quota* owed to them. The same rule proves, by way of consequence, that there is no possibility of dismantling the debtor's assets and their separate realisation, outside the bankruptcy proceedings.

In addition, an inequitable situation is set between current creditors enjoying a writ of execution and other current creditors.

Traditionally, opening of insolvency proceedings has as a core impact the *automatic stay*. In other words, it was held with justification that the insolvency proceedings represent a real impediment to the execution process, this being a reason for facing the dangerous situation in which guarantees are affected.

The action itself strongly affects the protection which has to be granted to financing operations within the proceedings, as the reimbursement of such financing operations is performed by bearing, pro rata, of an equal quota of assets subject to guarantee, by the pre-existing secured creditors.

Drawing a conclusion, the insolvency, by its reference fundamental principles, could be defined as a "relinquishing" of individual interests in favour of the equal and egalitarian interest of all the creditors, such an interest being managed by the practitioner in insolvency under the control of the syndic judge.

Effects of individual foreclosures, successively generated, affect even such fundamental principles and turn the insolvency proceedings into mere execution proceedings with no rules....

We are waiting, very interested, for the final version of the insolvency Code to be adopted by the Parliament. ■