

## Chapter 21

# Legal regime of real guarantees

## 1. General

Real guarantees are security interests that grant a secured creditor the right to recover its debt secured on the mortgaged or pledged assets, previously to any unsecured creditor and any other creditors with subsequent ranking security interests or other preference rights. Moreover, the secured creditor has the right to recover its debt irrespective of the holder of the secured asset (the right of pursuit).

Real guarantees fall into two large categories: real estate security interests (mortgages) and security interests on movable assets.

## 2. Main regulations

- The Civil Code;
- The Civil Procedure Code;
- Law no. 7/1996 on cadastre and real estate publicity with subsequent amendments and supplements (“Law no.7/1996”);
- Title VI of Law no. 99/1999 regarding certain measures for speeding up the economical reform (“Law no. 99/1999”), amended by Law no. 161/2003 regarding certain measures meant for corruption prevention and sanctioning.

## 3. Real estate security interests (mortgages)

### 3.1. Types of Mortgages

According to the Civil Code, a mortgage is a “real right in a property affected to the performance of the obligation undertaken”.

The Civil Code regulates two categories of mortgages: legal mortgages and conventional mortgages.

While a legal mortgage arises out of a special legal provision, a conventional mortgage arises out of an agreement between parties.

A mortgage shall be constituted by the owner of the immovable asset over such asset. An exception to the rule that mortgages cover immovable assets is the case of movable assets, such as vessels and aircrafts, over which mortgages can be placed, despite the fact that they are not generally considered immovable assets.

Also, as a rule, future assets cannot be mortgaged. However, an exception to this rule is provided by Law no. 190/1999 regarding the mortgage loan.

The mortgage contract must be concluded in authenticated form and it must set out both the mortgaged real estate and the amount of the debt secured by the respective mortgage, failing which the contract is null and void.

### 3.2. Mortgages registration formalities

In order to ensure ostensibility towards third parties and a preferential ranking thereof, certain real estate publicity formalities must be observed, namely the mortgage has to be registered with the Real Estate Registry<sup>1</sup>. The registration with the Real Estate Registry becomes ostensible towards third parties on the date of registration of the application for registration. The order of the registration application determines the registration rank, which plays an important role between categories of different rank creditors. The first to register the mortgage contract will prevail in recovering its debt over the other creditors. In case several applications are submitted at the same time with the same Real Estate Registry, the mortgage rights and privileges will take the same rank.

The effects of a mortgage registration cease after 15 years from the date of registration with the Real Estate Registry, unless registration is renewed. An exception to this rule was established by Law no. 190/1999 regarding the mortgage loan, whereby mortgages constituted to secure mortgage loans last until full repayment of such loan, thus no registration renewal after 15 years being necessary.

## 4. Security interests on movable assets

The regulatory framework on security interests on movable assets is contained in the Civil Code and was previously contained also in the Commercial Code. Although it endured the test of time since their respective enactments in the nineteenth century, the Civil Code and Commercial Code have not kept the pace with the new economical realities. This is why Law no. 99/1999 regarding certain measures for speeding up economic reform has instituted a uniform regulation for security interests on movable assets, meant to provide, *inter alia* enforcement obligations, especially in case of commercial obligations.

### 4.1. Traditional frameworks

The Civil Code provides as security interests the retention right and the pledge.

#### 4.1.1. The retention right

The retention right is viewed as an imperfect security right, based on which, the holder of a movable or immovable asset belonging to another person and which must be ultimately returned to that person, is entitled to retain that asset until the owner of the asset pays the expenses incurred with the asset maintenance, preservation and improvement. Said right operates only as long as the asset is in the holder's possession.

#### 4.1.2. The pledge

The pledge is an ancillary contract whereby the debtor hands over to the creditor a movable asset with the purpose to secure the obligations of the former towards the latter. The pledgor must be the owner of the pledged asset.

Generally, under the traditional legislation, the pledge mechanism involved the dispossession of the debtor of his asset.

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<sup>1</sup> The application for the registration with the Real Estate Registry will be submitted at the Land Registry Office of the mortgaged real estate is located.

## 4.2. Development in the law

### 4.2.1. General

The main amendments brought to the legal regime of security interests by Law no.99/1999 are as follows:

- It has extended the asset categories over which actual security interests may be created, by including intangible movable assets and future assets;
- It has clarified the legal status of security interests without dispossession;
- It has provided for the means of ensuring the security interests' ostensibility towards third parties by registration with the Electronic Archive of Movable Security Interests (the "Archive");
- It has introduced supplementary procedures for enforcement of security, by providing for the possibility for the creditor to take possession of the asset and to sell the same through a simple and cost-efficient procedure.

### 4.2.2. Security interest contract

According to Romanian law, security interests can be constituted only based on a security contract, concluded in authenticated form or under private signature or by other specific means in case of certain commodities traded on regulated markets (i.e. securities).

The applicable law provides the obligation to specify in the contract the maximum amount of the secured obligation. The contract must also contain a description of the pledged asset, in kind, asset by asset or by the general formula "all the debtor's present and future assets".

The security contract may have as object future assets and even assets universalities.

Such security produces effects only as of the date when the debtor receives title over the assets described in the contract.

The security contract may provide that the pledged asset secures a future obligation.

The security contract grants an enforcement *per se*.

Over the security contract duration, the debtor may manage or dispose in any legal way of the secured asset and of its proceeds, including leasing it, creating another security interest or selling it. The acts of disposal over the pledged asset are valid, even if the person receiving the title over the asset was aware of the contract provision according to which such disposal acts are forbidden or which declares such disposal an event of default.

The above-mentioned legal provision is meant to ensure free circulation of assets. Having the right of pursuit over the pledged asset, the creditor is secured even if the debtor alienates such assets, as he can trace it in the hands of whoever possesses it. Yet, nothing prevents the creditor from introducing in the security contract a provision stating that the transfer constitutes event of default under certain circumstances provided for in the contract. Such a provision is legal and produces effects, but it may not invalidate the transfer of the pledged asset.

### 4.2.3. Publicity of security interests

The priority of a security interest begins on the moment when a "security notice" is registered with the Archive.

The Archive is a record system regarding the priority and publicity of security interests, structured on persons and assets. The Archive is a public system and its access is free of charge.

The persons attending to conclude and register security contracts may at first register with the Archive the intention to set up a security. The registration of the intention produces effects only for a period of 2-months as of registration. Once the security constituted and registered within the 2 months, it will gain retroactive priority as of the date of the registration of the intention. The security notice is valid for a period of 5 years as of the registration date.

Each creditor is bound to send a copy of the security registration notice to the debtor, within maximum 24 hours as of the registration of the notice.

Within 40 days as of the security contract termination, the creditor must submit a notification to such effect to the Archive.

#### **4.2.4. Enforcement of the security interests**

In case of failure to fulfill the secured obligation, the creditor is entitled to amicably take possession over the pledged asset or the proceeds resulted from its sale, as well as of the documents and deeds attesting the debtor's title to the asset, without requiring a prior authorization or notice and without paying any taxes or fees.

Public clerk or police officers may not accompany the creditor during the amicable taking possession over the asset. The law provides that, in order to amicably take possession over an asset, the security contract must include the following formula, written in capital letters, of at least font 12 (0.5 cm): "in case of default, the creditor may use its own means in order to take possession over the pledged asset".

If taking possession over the pledged asset is not possible in an amicable manner, the secured creditor may ask for the support of a court bailiff, or, as the case may be, of the bank liquidator or of any other competent body. Within 48 hours as of the receipt of such request, the bailiff will go to the place where the pledged asset is located, will take possession thereto and will deliver it to the creditor.

If the debtor fails to observe its obligation and disposes of the pledged asset or grants rights over the asset, the creditor is entitled to exercise its right over the pledged asset, which is in the possession of a third party, or over the proceeds resulting from such asset, or over both. Any asset replacing the pledged asset or its corresponding value will be presumed to be the product of the initial asset, except for such cases where the debtor proves otherwise.

The parties may agree, based on the security contract, on the capitalization methods of the pledged assets, in case of failure to perform the secured obligation. In the absence of such an agreement, the creditor will be bound to sell the asset by reasonable commercial means.

The buyer will take possession of the pledged asset, free from any security interests and other encumbrances.

Before the sale, under the sanction of voidance and liability for the damages caused, the creditor has to send a sale notification both to the debtor and to the other creditors who have registered a security notice against the same debtor and over the same asset, and to the owner of the pledged asset, if the debtor is no longer the asset owner.

The creditor cannot take possession over the pledged asset within a sale initiated by itself, without first offering to third parties the possibility to participate in the sale, except for such cases when the parties agree otherwise.

If the pledged asset is sold, the creditor shall distribute the sale proceeds as follows (art. 78 from Law no. 99/1999):

- a) payment of any expenses resulted from the maintenance, conservation, taking possession and sale of the asset;
- b) payment of the interests and of the secured obligation which have a superior priority ranking, even if the same have not become due.

Any outstanding amounts remained, after the debt of the creditor ranking highest in terms of priority is covered, will be distributed to the other creditors according to their priority rank, even if their debts have not yet fallen due. Only after full payment of one creditor, the payment of other creditors may be initiated.