

## Chapter 5

# Insolvency

## 1. General

Currently, in Romania, the insolvency procedure is in line with modern standards, based on two significant commercial principles typical for any free market economy, as follows:

- (i) the attempt to recover the company through reorganization;
- (ii) the organization of bankruptcy proceedings in a manner enabling the creditors to recover their receivables in as much as possible.

Even though not all creditors are satisfied with the order in which these two principles are applied, the benefits of the current insolvency legislation are obvious. In fact, the major breakthrough was made by the implementation of former Law no. 64/1995, taking into account that the previous provisions were to a certain extent covered by the Commercial Code and the Civil Code, some in force since the 19<sup>th</sup> century.

As of 2006, Romania has a new law that regulates the insolvency procedure, *i.e.*, Law no. 85/2006 on insolvency procedure, which replaced the former Law no. 64/1995 on judicial reorganization and bankruptcy procedure.

At present, one can say that Romania has modern insolvency regulations, adapted to the period of economic transition that Romania has been crossing during the last decade. However, the Romanian authorities have to continue improving these regulations in order to meet the developments and changes that the Romanian business environment is constantly undergoing.

## 2. Main regulations

- Law no. 85/2006 on insolvency procedure, as further amended and supplemented (“Law no. 85/2006”);
- Government Ordinance no. 10/2004 on the bankruptcy procedure of credit institutions, approved by Law no. 278/2004, as further amended and supplemented (“GO no. 10/2004”);
- Law no. 503/2004 on financial recovery and bankruptcy of the insurance companies;
- Council regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings;
- Law no. 637/2002 regulating the international private law relations concerning insolvency, as further amended and supplemented (“Law no. 637/2002”).

### 3. Entities subject to insolvency procedure

#### 3.1. Entities subject to general insolvency procedure

**3.1.1. Corporate entities** organized and carrying out business in accordance with Company Law no. 31/1990, as further amended and supplemented, including subsidiaries of foreign companies.

**3.1.2. Cooperative companies**

**3.1.3. Cooperative organisations**

**3.1.4. Agricultural undertakings**

**3.1.5. Groups of economic interest** (as regulated by Law no. 161/2003, as further amended and supplemented).

**3.1.6. Any other private legal person that carries out economic activities**

#### 3.2. Entities subject to simplified insolvency procedure

**3.2.1. Traders, natural persons, who act individually**

**3.2.2. Family associations**

**3.2.3. Debtors** mentioned at point 3.1. above that comply with one of the following conditions: (i) they have no asset in their patrimony; (ii) their articles of association or accounting documents cannot be found; (iii) the director may not be found; (iv) the headquarters no longer exists or no longer corresponds to the address in the Trade Registry.

**3.2.4. Debtors** provided at point 3.1. above that did not timely submit with the court certain documents set forth by Law no. 85/2006.

**3.2.5. Corporate entities** dissolved prior to filling the claim for opening the insolvency procedure.

**3.2.6. Debtors** that have declared in the claim filed with the courts their intention to undergo bankruptcy or those which are not entitled to undergo judicial reorganization procedure.

### 4. Mandatory conditions for the commencement of the insolvency procedure

Law no. 85/2006 sets forth two mandatory conditions, which need to be cumulatively met in order for the creditors to be able to commence the insolvency procedure against their debtor:

- (i) the creditor has a certain, liquid and outstanding receivable against the debtor for more than 90 days;

- (ii) the receivable must exceed the amount of RON 45,000, or 6 national gross average salaries/per employee, for receivables arisen out of labour relations.

The debtor itself is compelled to submit a claim for the commencement of the insolvency procedure within 30 days as of the date the state of insolvency has occurred. In the meaning of Law no. 85/2006, insolvency refers to the insufficiency of the available funds for the payment of certain, liquid and outstanding debts, as follows:

- (i) the state of insolvency is presumed as obvious when the debtor, after 90 days as of the maturity date, failed to pay its debt towards the creditor; such presumption is relative meaning that a proof to the contrary is admissible;
- (ii) the state of insolvency is reputed to be imminent if it can be proved that the debtor will not be able to pay its outstanding debts with the available liquidities on the maturity date.

## 5. Procedures

Law no. 85/2006 regulates two procedures to be undertaken by debtors who are not able to pay their dues provided that the conditions at point 4 above are met:

- (i) the judicial reorganization procedure, aiming to rescue the debtor;
- (ii) the bankruptcy procedure aimed at liquidating debtor's assets and paying all outstanding debts.

Likewise, Law 85/2006 sets forth another classification of the insolvency procedures as follows:

- (i) the general insolvency procedure applying to the debtors mentioned at point 3.1. above; such entities shall undergo successively, the judicial reorganization procedure and the bankruptcy procedure or, separately, on a case by case basis, only the judicial reorganization procedure or bankruptcy procedure;
- (ii) the simplified insolvency procedure applying to debtors mentioned at point 3.2. above; such entities shall directly undergo the bankruptcy procedure.

### 5.1. Judicial reorganization

In case of judicial reorganization, after confirmation of the reorganization plan, the debtor's business will be managed by the special administrator under the supervision of a receiver (judicial administrator) appointed by the syndic judge. The special administrator is appointed by the debtor's general meeting of shareholders. The syndic judge may decide to withdraw, entirely or partially, the special administrator's powers of managing the debtor's business.

The debtor will also be subject to a reorganization plan, envisaging specific means of paying the outstanding debts. If such reorganization plan is successful, the debtor will continue its activity. In case the debtor fails to

comply with the reorganization plan or such plan is not successful, the syndic judge may approve the commencement of the bankruptcy proceedings.

In practice, the judicial reorganization procedure is applied more and more frequently.

## 5.2. Bankruptcy

The bankruptcy procedure shall be applied in the following cases:

- (i) the debtor expressed its intention to undergo the simplified procedure;
- (ii) the debtor did not express its intention to reorganize its activity;
- (iii) the debtor's objection to the creditor's request to commence the insolvency procedure was rejected by the syndic judge;
- (iv) none of the entitled persons proposed a reorganization plan or the proposed plan was not accepted and confirmed;
- (v) the debtor expressed its intention to reorganize its activity, but did not propose a reorganization plan or the proposed plan was not accepted and confirmed;
- (vi) the payment obligations and other incumbent obligations are not accomplished according to the conditions stressed in the reorganization plan or the activities carried out by the debtor during the reorganization procedure trigger losses to its patrimony;
- (vii) the receiver's report proposing the commencement of the bankruptcy procedure was approved.

There are several stages to be observed in a bankruptcy procedure starting with the identification of debts and creditors, followed by the liquidation and the distribution of the proceeds obtained from liquidation. The main stages of the bankruptcy procedure are the following:

- (i) withdrawing debtor's right to manage its business;
- (ii) preparing an inventory of debtor's assets;
- (iii) appointing a temporary liquidator within the general procedure which has to be further confirmed, and confirming, as liquidator, the receiver within the simplified procedure;
- (iv) establishing liabilities: drawing up the list of creditors, the list of debtor's assets and the profit-and-loss account for the year prior to the date of filing the bankruptcy application, verifying the creditors' receivables and drawing up the list of receivables, settlement by the syndic judge of any objections, drawing up and posting the final chart of the debtor's liabilities;
- (v) carrying out the liquidation: sale of the debtor's assets by auction or by direct sale (wholesale or retail), payment of taxes, stamp duties and all sale-related expenses, payment of secured creditors

(the secured creditors are such creditors who have mortgages, pledges, or retention rights on debtor's assets);

- (vi) distributing the amounts resulted from liquidation: drawing up the final report and balance sheet by the liquidator, settlement of the objections thereof and approval of the same by the syndic judge and final distribution of the debtor's funds with the observance of the priority order set forth by the law;
- (vii) closing the liquidation process, upon the liquidator's request, conveyed in a decision of the syndic judge.

From practical experience it was noted that, in general, creditors have to wait around one year or even more until the bankruptcy procedure is closed and they can actually recover their receivables (such term does not include a potential prior reorganization procedure which might extend up to maximum 3 years as of the confirmation of the reorganization plan).

## **6. Official bodies implementing the insolvency procedure**

According to Law no. 85/2006, such official bodies are the court, the syndic judge, the creditors' assembly, the special administrator, the receiver/judicial administrator and the liquidator. The syndic judge has mainly coordination tasks, while the administrator/receiver/liquidator have mainly executive duties. Insolvency practitioners, entities or individuals, carry out the reorganization and liquidation activity.

### **6.1. The court**

All main proceedings regarding judicial reorganization and bankruptcy, except for second appeals filed against the decisions of the syndic judge which are settled by the court of appeal, are under the exclusive competence of the tribunal having jurisdiction within the county where the debtor's headquarters are located. The syndic judge is randomly selected through a computerized system amongst the specialized judges within the respective tribunal.

### **6.2. The syndic judge**

The main attributions of the syndic judge are as follows:

- (i) to decide upon commencement of the insolvency procedure, both general as well as simplified procedure;
- (ii) to appoint or, as the case may be, replace the temporary receiver or liquidator and set forth their attributions;
- (iii) to confirm the receiver or the liquidator appointed by the creditors' assembly;
- (iv) to examine the legal actions filed by the receiver or liquidator;
- (v) to settle the potential objections filed by the creditors, by the debtor or of any other persons;

- (vi) to decide upon the closing of the insolvency procedure.

### **6.3. Creditors' assembly**

The creditors' assembly is formed by the debtor's creditors and is convened and chaired by the receiver or liquidator (unless the law or the syndic judge requires otherwise). The creditors' assembly may be also convened at the request of the creditor's committee or at the request of creditors holding at least 30% of the total value of receivables.

The creditors' assembly may appoint during their first meeting a creditors' committee formed of 3 or 5 creditors of the first 20 creditors based on the amount of the debts; the committee thus appointed will replace the committee that might have been previously appointed by the syndic judge.

The main attributions of the creditors' committee are as follows:

- (i) to analyse debtor's financial status and to make proposals to the creditors' assembly on debtor's activity;
- (ii) to analyze the reports drafted by the receiver or liquidator and, as the case may be, to challenge such reports;
- (iii) to draft reports on the measures taken by the receiver or by the liquidator, to present said reports to the creditor's assembly and make new recommendations if the case;
- (iv) to request the withdrawal of the debtor's right to manage its business.

### **6.4. Special administrator**

Following the commencement of the procedure, the debtor's general meeting of shareholders will appoint, on the shareholders' expenses, a representative as special administrator, in order to represent the debtor's interests as well as the shareholders' interests and to participate in the procedure on behalf of the debtor. Following the withdrawal of the debtor's right to manage its business, the debtor will be represented by the receiver/liquidator who will also manage its activity while the mandate of the special administrator will be reduced to representing only the shareholders' interests.

The main attributions of the special administrator are the following:

- (i) to express the debtor's intention to enter into the bankruptcy procedure or to reorganize its activity;
- (ii) to propose a reorganization plan;
- (iii) to manage debtor's activity under the supervision of the receiver after the confirmation of the plan;
- (iv) to participate to the inventory following the commencement of bankruptcy procedure;

- (v) to receive the final report and the closing balance and to participate in the meeting convened for the settlement of the objection and approval of the final report.

### **6.5. The receiver**

The creditor holding at least 50% of the total value of the receivables or, as the case may be, the creditors' assembly with a majority of minimum 50% of the total value of the receivables may decide the election of a receiver (natural person or legal entity), and fix his remuneration, save for the case when such remuneration shall be paid out of the liquidation fund case in which the syndic judge sets forth the amount thereof.

The receiver, natural or legal person, as well as the representative of the latter must be an authorized practitioner in insolvency.

The receiver's main attributions are the following:

- (i) to elaborate the reorganization plan;
- (ii) to manage debtor's business activity;
- (iii) to file actions for declaring void any fraudulent acts, concluded by the debtors and causing damage to the creditors' rights, as well as certain asset transfers and business operations entered into by the debtor and the setting up of guarantees likely to prejudice the creditors' rights;
- (iv) to maintain or terminate certain contracts concluded by the debtor;
- (v) to conclude transactions, waiver of debts and personal guarantors, relinquish security interests upon the confirmation by the syndic judge.

### **6.6. The liquidator**

In case the syndic judge decides upon the commencement of the bankruptcy procedure, a liquidator shall be appointed. Such liquidator may also be the former receiver.

The main attributions of the liquidator are:

- (i) to manage debtor's activity;
- (ii) to file actions for declaring void any fraudulent acts, concluded by the debtors and causing damage to the creditors' rights, as well as certain asset transfers and business operations entered into by the debtor and the setting up of guarantees likely to prejudice the creditors' rights;
- (iii) to sell the assets of the debtor;
- (iv) to conclude transactions, discharge debts, discharge the personal guarantors, relinquish security interests, all upon confirmation of the syndic judge.

One of the most important attributions for both the liquidator and the receiver is filing actions aimed to annul deceptive acts concluded by the debtor. Thus, no later than 16 months as of the date of commencement of the insolvency procedure the court may be invested to declare void the agreements the debtor has entered to the detriment of creditors, during the last 3 years prior to the commencement of the procedure.

## **7. Banking bankruptcy**

Credit institutions duly incorporated in Romania, their subsidiaries abroad and the credit cooperatives (called hereinafter “credit institutions”), undergoing an insolvency state, are subject to special bankruptcy proceedings instituted under GO no. 10/2004.

Credit institutions are deemed insolvent if in one of the following situations:

- (i) in case of manifest incapacity of paying its outstanding debts with the available liquidities;
- (ii) the solvency indicator (calculated based upon the relevant regulations issued by the National Bank of Romania) drops under 2%;
- (iii) in case of withdrawal of the operating license, due to the impossibility of being financially restored.

If insolvent, credit institutions have the obligation to request the relevant court, within 30 days, to commence the bankruptcy procedure. Prior to such request, the credit institutions have to file a request within 10 days as of the insolvency interfered with the National Bank of Romania in order to obtain the approval on the commencement of the bankruptcy procedure.

Creditors of the insolvent credit institution may also file a bankruptcy request in the following cases:

- (i) the central houses of credit cooperatives, including the credit cooperatives affiliated thereto, have not fully paid their certain, liquid and outstanding debts within at least 30 days as of maturity date;
- (ii) other credit institutions (including banks) have not fully paid their certain, liquid and outstanding debts within at least 7 days as of maturity date.

The file of the bankruptcy request in both cases provided above has to be preceded by the prior approval of the National Bank of Romania.

The bankruptcy procedure starts following an application filed by the debtor, by its creditors or the National Bank of Romania.

All main procedures provided by GO no. 10/2004, except for second appeals which are settled by the court of appeal, are under the exclusive competence of the tribunal, which has jurisdiction within the county where the debtor’s headquarters are located. The syndic judge shall be randomly selected through the computerized system amongst the specialized judges within the respective tribunal.

The court will notify the National Bank of Romania on its decision to start the bankruptcy procedure for each relevant credit institution. The National Bank of Romania will immediately close the accounts of the relevant credit institution opened with the National Bank of Romania and transfer the available funds into the accounts of “*credit institution in bankruptcy*”-type opened by the liquidator with a commercial bank where all other available funds of the debtor shall be transferred as well. Subsequently, the financial operations of the bankrupt credit institution shall be undertaken through this account exclusively.

Subject to approval of the final report by the syndic judge, the distribution of all funds or assets of the bankrupt credit institution and depositing of all unclaimed funds with the Romanian Treasury and the submission of the statement of accounts with the syndic judge, the insolvency procedure shall be closed. The decision to close the bankruptcy procedure is notified, in writing or through the media, to all involved parties.

## **8. International private law relations regarding insolvency**

### **8.1. Harmonized EU insolvency rules (source: European Commission)**

As of the Romanian accession to the European Union (“EU”) in 2007, the international private law aspects regarding insolvency are mainly regulated by the Council regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings (the “Regulation”).

The Regulation establishes a common framework for insolvency proceedings in the EU. The purpose of harmonised arrangements regarding insolvency proceedings is to avoid assets or judicial proceedings from being transferred from one EU country to another in order to obtain a more favourable legal position to the detriment of creditors (“forum shopping”).

Except for insurance undertakings, credit institutions and collective investment undertakings, the Regulation applies equally to all proceedings, whether the debtor is a natural or a legal person, a trader, or an individual.

According to the Regulation, the courts with jurisdiction to open the main insolvency proceedings are those of the EU country where the debtor has his/her centre of main interests. This should be the place where the debtor usually administers his/her interests and that is verifiable by third parties. In the case of a company or legal person, this is the place of the registered office, in the absence of proof to the contrary. In the case of a natural person, in principle it is the place where his/her work is domiciled or the place of his/her usual residence.

Secondary insolvency proceedings may be opened subsequently in another EU country if the debtor has an establishment in its territory. “Establishment” means any place of operations where the debtor carries out a non-transitory economic activity with human resources and goods. The effects of the winding-up proceedings must be limited to the assets of the debtor located in that territory. The opening of such proceedings may be requested by the liquidator of the main proceedings or by other persons or authorities according to the law of the country in which the opening of the proceedings is requested. In some cases, such territorial proceedings may be opened independently before the main proceedings, if the local creditors and the creditors of the

local establishment request it or where main proceedings cannot be opened under the law of the EU country where the debtor has his/her centre of interests. However, these proceedings will become secondary proceedings once the main proceedings are opened.

Pursuant to the Regulation, the law of the EU country in which insolvency proceedings are opened determines all the terms of those proceedings: the conditions for their opening, conduct and closure. It also determines practical rules such as the definition of debtors and assets, the respective powers of the debtor and the liquidator, the effects of proceedings on contracts, individual creditors, claims, etc.

Decisions by the court with jurisdiction for the main proceedings are to be recognised immediately in other EU countries without further scrutiny, except:

- (i) where the effects of such recognition would be contrary to the country's public policy;
- (ii) in the case of judgments that might result in a limitation of personal freedom or postal secrecy.

However, restrictions on creditors' rights (a stay or discharge) are possible only if they have given their consent.

If a court of an EU country decides to open insolvency proceedings, the decision is to be recognised in all other EU countries, even if the debtor could not be the subject of such proceedings in the other countries. The effects of the decision are those provided for by the law of the country in which proceedings are opened and they come to an end in the event of secondary proceedings being opened in another EU country.

The liquidator appointed by a court with jurisdiction may act in the other EU countries in accordance with his powers provided for by the law of the EU country where the proceedings are opened, but respecting the law of the country on whose territory s/he is acting. In particular, s/he may have the debtor's assets removed and may bring any action to set aside that is in the interests of the creditors if assets were removed from the country of the main proceedings after the opening of the proceedings, subject to rights in rem of third parties or reservation of title.

Publication measures may be taken in any other EU country at the request of the liquidator (publication of the decision opening the insolvency proceedings and/or registration in a public register). Publication may be mandatory, but in any event it is not a prior condition for recognition of the foreign proceedings.

If a person concerned is not aware of the opening of proceedings, s/he may be considered to act in good faith when making a payment to the debtor instead of the liquidator in another EU country. If such a payment is made before publication of the decision opening the proceedings, the person concerned is considered to have been unaware of the opening of proceedings. On the other hand, if a payment is made after publication of the decision, the person concerned is assumed to have been aware unless there is proof to the contrary.

## 8.2 Subsequent Romanian insolvency related enactments on international private law

In international insolvency related aspects where the aforementioned Regulation is not applicable it shall be applied the Law no. 637/2002 which contains provisions meant at (i) establishing the law applicable to private international relations on insolvency, (ii) outlining applicable procedural norms in private international relations on insolvency, and (iii) setting forth the conditions to be observed by the Romanian relevant authorities when requesting/giving assistance in respect of insolvency proceedings commenced on the Romanian territory/foreign territory.

Under the Law no. 637/2002 usually the law applicable to private international relations in terms of insolvency is the law applicable at the debtor's central headquarters, namely the law applicable in the area of the main headquarters of a legal entity or the law of the professional domicile of the natural person performing an economic activity or an independent profession.

Law no. 637/2002 mainly regulates the following scenarios:

- (i) cases when legal assistance is required in Romania by a foreign court or by a foreign representative, in respect of a foreign insolvency procedure

Such cases may occur when the insolvency procedure has started abroad and its recognition in Romania is required (for example, because the debtor has assets located in Romania).

In such cases, the foreign representative has the right to address directly to the Romanian courts and bring before them a recognition petition for the foreign procedure, by also submitting several documents in order to prove the commencement of the procedure abroad.

If the Romanian courts admit the foreign procedure, no other further individual petitions and appeals or enforcement measures, judicial or extrajudicial may be brought before the court, and if they have already been started they shall be suspended. Furthermore, the right to charge or dispose in any way of the debtor's assets will be suspended. Any deeds failing to comply with these rules will be null and void.

- (ii) cases when legal assistance is required in a foreign state, in respect of a bankruptcy procedure governed by Romanian law

This situation occurs when the bankruptcy procedure starts in Romania and its recognition abroad is required (for example, because the debtor has assets located abroad).

The Romanian representative (the individual or legal person appointed receiver or judicial liquidator within a Romanian bankruptcy procedure) is entitled to act in a foreign state, as delegate of the bankruptcy procedure opened in Romania, under the conditions set forth by the foreign applicable law.

- (iii) cases when a Romanian insolvency procedure and a foreign insolvency procedure against the same debtor are carried out simultaneously

In this particular case, admittance of the foreign procedure cannot prevent filing of a local action under Law no. 85/2006, or the registration of an application for claim admittance under such procedure.

After recognition of a foreign procedure, the insolvency procedure regulated by Law no. 85/2006 may be commenced against the same debtor only if the debtor is headquartered in Romania. The effects of the procedure provided by Law no. 85/2006 shall be limited only to the debtor's assets located in Romania and to other assets which, pursuant to the Romanian law, have to be covered by such procedure, to the extent imposed by the need to ensure cooperation between the Romanian and foreign authorities. The recognition of a foreign procedure is, until proven otherwise, an assumption of the debtor's insolvency and the procedure provided by the Law no. 85/2006 may be started based on this assumption.