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ARTICLE

The Recent Reforms in the Romanian Insolvency Law

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The Romanian Government has recently taken several steps to modernise and simplify Romanian insolvency law, with a view to increasing the effectiveness of the insolvency proceedings. The result is a comprehensive set of updated insolvency rules in one single law, an enhanced protection of certain creditors and a strengthened out-of-court restructuring process.

The insolvency law is one of the most important pieces of regulation and in the last 20 years we have witnessed a legislative roller-coaster in the insolvency field in the attempt to align the local norms to the European standards.

Statistics indicate that successful restructuring proceedings in the insolvency files are quite rare and the complex effort to align the frequently conflicting interests of the parties fails almost every time because of the 'no compromise' policy of the creditors.

In Romania, the insolvency process is still associated with fraudulent debtors, vengeful creditors, biased insolvency practitioners, overloaded insolvency courts and syndic judges with questionable reputation.

After numerous amendments to the insolvency law that have taken place over the last 20 years, the Romanian Government adopted on 2 October 2018 the Emergency Ordinance 88/2018 amending the insolvency law once again.

The Romanian government took into account, when adopting this law, the need for efficient mechanisms for recovering the budgetary receivables from companies in the insolvency procedure, but with the chances for such companies to recover from financial difficulties and continue their activities.

Moreover, it is considered the need to take measures against the disturbance of the competitive environment by operating the insolvency procedure abusively by some debtors who use this procedure in order to avoid paying the amounts due to the general budget.

One of the major changes of the insolvency law is to forbid the initiation of the insolvency when the companies owe more than 50% of their debt to the state.

According to the Ministry of Finance, the main purpose for which this law was adopted is to stop the fraudulent insolvency, but specialists have warned that the changes will also produce collateral victims, such as those companies who are likely to pass from insolvency directly to bankruptcy. In addition to that, highly respected commentators have implied that this new legislative effort if centred on the increased power of the Ministry of Finance to accelerate the collection of the budgetary debt and sanction, in the same time, the insolvent media groups supporting the political opposition.

These changes have come in the current context in which the number of the companies that have entered into insolvency has greatly increased, reaching more than 6,000 companies in the insolvency procedure.

In relation to the provisions that establish a fast procedure for checking the current receivables, respectively the transition to the bankruptcy procedure, the purpose is to reduce the risk to accumulate budgetary debts during the insolvency period.

However, there is a risk that such changes will not lead to an effective increase in recovering the budgetary debts, but rather to a larger exposure of the creditors.

In the following we will present the main changes of the insolvency law.

A first provision refers to an additional condition for the debtor to initiate the insolvency procedure. Thus, besides the debt's threshold-value which is set to RON 40,000 for an interested person to request the initiation of the insolvency procedure, in case of a self-insolvency application, the amount of budgetary debts must be less than 50% of the total debts that are declared by the debtors. In conclusion, there will be a double condition regarding the threshold-value.

This will lead to a postponement of the debtor's request for the initiation of the insolvency, for those companies that do not fulfil the necessary conditions. Thus, even if the companies fulfil other conditions for the insolvency, they will not be able to initiate the procedure, because of the non-fulfilment of the new threshold condition stipulated by the law. This will conduct to a greater deterioration of the debtor's financial situation and the chances of reorganisation will be significantly reduced.

Likewise, there is also a possible issue of unconstitutionality regarding the double-threshold, as it may harbour a discrimination between private and public creditors who already have a privileged treatment in respect of the priority rank in the Creditor's Table, the challenge of the claim and the order of distribution according to the insolvency law provisions.

The creditor, who also has the position of special administrator, is forbidden to vote for decisions regarding the current activity of the debtor. In this respect, the law stipulates the sanction for violating such provision, in which case the decision may be annulled by the syndic judge.

The new law regulates the incompatibility between a Committee member or a special administrator with the status of creditor.

A new provision is implemented regarding the possibility to sanction the insolvency practitioner by forcing him to pay any expenses, fines, damages or any other amounts of money if in his position of legal representative of the debtor, he does not adequately fulfil his duties, and this sanction may be applied by the court or by any other authority for its acts or omissions.

Regarding the report which is drafted by the judicial administrator, the Emergency Ordinance updated the provisions related to its content which should also include from now on the description of the way the judicial administrator carried out the tasks, such as: information on any operations that are performed upon the preliminary notice, the expenses that emerge from the judicial administrator's activity, relevant aspects on the payment of the tax liabilities, including those related to the authorisations or permits necessary to carry out the activity, etc.

Additional criteria regarding the implementation of a reorganisation plan by the fiscal creditors were regulated, increasing exponentially the effort to secure the approval of the reorganisation plan.

Another amendment introduced by the Emergency Ordinance no. 88/2018 concerns the activity of the judicial administrator and it aims at designating the specialists with whom he may cooperate during the insolvency procedure.

The judicial administrator will not be able to appoint persons who are in a contractual or affiliate relationship with the legal administrator, the liquidator or with the insolvency debtor or any of the creditors, such as lawyers, accountants, assessors or other specialised professions. This amendment puts an abrupt end to the potential conflict of interest triggered by the professional cooperation between judicial practitioners and third parties services providers. Many of the insolvency practitioners in Romania are registered lawyers and they have to retain legal serviced during the insolvency proceedings. In the past, this situation generated many conflicts of interest as the judicial practitioners retained themselves or related parties as legal counsels.

Another important provision was implemented regarding the settlement of the bankruptcy request, as follows: if the debtor does not comply with the reorganisation plan or if he accumulates new debts to the creditors in the insolvency procedure, any creditor or the administrator may request the syndic judge to initiate the debtor's bankruptcy. The request shall be judged urgently within 30 days of its registration. The request shall be rejected by the syndic judge in the event that the claim is not due, is paid or the debtor concludes a payment agreement with the creditor. For those debts which are accumulated during the insolvency procedure and which are older than 60 days, the enforcement procedure can be initiated.

Also, the holder of a current debt may request the initiation of the bankruptcy at any time during the reorganisation plan or after the payment of the obligations in accordance to the plan if his debt is certain, liquid, outstanding, older than 60 days and it is an amount above the threshold value. The claim shall be judged urgently and in particular within 30 days of its registration in the case file. The claim will be rejected by the syndic judge in the case that the debt is not due, is paid or the debtor concludes a payment agreement with the creditor.

These amendments represent a fast-track procedure to liquidate insolvent companies and, although the norms are meant for a general application, debtors are worried that the budgetary creditors are going to pull the trigger only against insolvent companies targeted based on arbitrary criteria.

A new amendment to the Insolvency Law refers to the conversion of the company's debt into shares to be transferred in the creditors' patrimony. The principle was regulated before, however the new amendments indicate for the first time a clear path for the budgetary debt equity swap. The specialists indicate that this procedure may allow the Ministry of Finance to hostile takeover insolvent media groups supporting the pollical opposition.

Finally, one of the most expected amendment introduces the budgetary receivables assigning procedure. The assignment of budgetary receivables was provided in a secondary legislation norm, however its applicability was quite limited as the budgetary creditors had to initiate the assignment procedure. In addition to that, the budgetary creditors were quite reluctant to use this collection tool in the insolvency files. Now that the Government explicitly regulated the budgetary receivables assignment procedure (for a minimum face value price and a maximum three years payment term), we do expect an increase in the assignment volume for budgetary receivables.

In the European legislation, there is no material difference between the situation of the budgetary creditors and other creditors, they should have a similar treatment and not being part of a favoured class of the creditors.

All these changes to the insolvency law are made only in favour of the budgetary creditors and, therefore, raise an unconstitutionality question mark. At the same time, they violate the principles set by the European legislation. Usually, the creditors must have the same rights in the insolvency procedure.

Therefore, as a result of the changes, the already existing preferential treatment of the budgetary creditors was exponentially enhanced, in the detriment of the other creditors which are participating in the insolvency procedure.

In conclusion, we believe that the budgetary debt-equity swap may provide on the short run some financial shelter for the insolvent companies, however, on the medium and long term this approach may prove completely futile as the State completely lacks the capacity to successfully implement the turnaround management for so many companies.

We consider that the state takes the risk of losing those amounts, rather than recovering them. The only possible benefit that could result from the debt conversion process is the attempt to save the jobs of the employees. However, in the absence of a sound reorganisation plan and professional turnaround management in the end the companies will most likely go bankrupt.

Unfortunately, many of these changes to the insolvency law are criticised and these legislative innovations do not exist in any European legal practice. We hope that the contradictory provisions will be clarified by the insolvency courts' practice.

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