APPROACHING INSOLVENCY FROM A EUROPEAN PERSPECTIVE

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Abstract. The increased number of companies and individuals from the EU that established business activities in other countries than the origin one has draw attention to insolvency and their specific procedures from the European Union. In order to develop a common framework for insolvency proceedings in the EU, the Council set up a Regulation on insolvency proceedings in which establishes the common rules that should be respected in this field. The present article focuses on the specific guidelines of EU Regulation regarding insolvency: court competence to open insolvency proceedings, the applicable law and the recognition of the court's decisions when a debtor becomes insolvent. Furthermore, it compares the EU Law on insolvency with the New Romanian Law on insolvency adopted in 2014, pointing out the main differences between them. The results show that both approaches concentrate on helping businesses overcome financial difficulties, all the while protecting creditors' right to get their money back.

Keywords: EU insolvency Regulations, Romanian insolvency law; insolvency proceedings, reorganisation, creditor's right

Introduction

Companies and individuals in the EU are increasingly establishing business activities or economic interests in EU countries other than where their core activities are located. If they become insolvent, there may be direct implications on the proper functioning of the internal market. To establish a common framework for insolvency proceedings in the EU, the Council set up a Regulation on insolvency proceedings that establishes common rules on:[1]

1. the court competent to open insolvency proceedings;
2. the applicable law;
3. the recognition of the court's decisions when a debtor (a company, a trader or an individual) becomes insolvent.

The main objective is to avoid the transfer of assets or judicial proceedings from one EU country to another, which can improve the legal position of companies or individuals.

European rules on cross-border insolvency are laid down in Regulation (EC) No 1346/2000 on insolvency proceedings (the "Insolvency Regulation"), which has applied since 31 May 2002. The Regulation contains rules on jurisdiction, recognition and applicable law and provides for the coordination of insolvency proceedings opened in several Member States. The Regulation applies when the debtor has an establishment or creditors in another Member State than his own.

Taking into consideration that the rules on cross border insolvency date from 2000, the Comission issued in 2014 a set of new recommendations that focus on helping businesses overcome financial difficulties, all the while protecting creditors' right to get their money back[2]. Furthermore, we are going to review the recommendation of the European Commission.

[1] http://ec.europa.eu/justice/civil/commercial/insolvency/index_en.htm, accessed in November 2014.
[2] European Commission, COMMISSION RECOMMENDATION of 12.3.2014 on a new approach to business failure and insolvency, http://ec.europa.eu/justice/civil/files/c_2014_1500_en.pdf, accessed November 2014.

1. EU's insolvency regulations

The European Commission believes there are three main reasons why insolvency laws are overdue for reform. The first is that in many countries they currently do not favour the early restructuring of companies in difficulties, which often leads to liquidation of viable enterprises. The second is that, under personal bankruptcy rules, "honest entrepreneurs" are not discharged quickly enough from their debts to try and build new firms. A third concern is that insolvencies involving cross-border organisations are often chaotic, as different countries have different rules and no one knows which ones have priority. Both entrepreneurialism itself and the amount of credit provided to entrepreneurs would be higher; the argument goes, if businessmen and their backers could count on a speedy and predictable outcome if the worst comes to the worst.[3]

The Commission's proposal to amend the Insolvency Regulation addresses many of the issues identified as problematic in a 2011 resolution of Parliament, in particular group insolvency, but does not go as far as harmonising national rules. In October 2011, the Parliament adopted an initiative report on insolvency proceedings, calling for partial harmonisation of insolvency law, a reformulation of COMI to prevent fraudulent forum-shopping, enactment of rules on insolvency of groups of companies and the creation of an EU insolvency register.

In December 2012, the Commission adopted a proposal to amend the Regulation. It would broaden its scope to cover not only bankruptcy, but also restructuring aimed at avoiding liquidation. A new, more precise definition of COMI would be introduced, codifying the clarifications from the case-law of the Court of Justice. Upon the lodging of insolvency proceedings, a court would have to verify whether it is competent under the Regulation, and foreign creditors would have the possibility to challenge that finding. The proposal would also address the issue of publicity and transparency, by obliging MS to create insolvency registers, embedded in the e‑Justice portal, and to publish relevant court decisions. New, detailed rules would oblige courts and liquidators from different MS to cooperate closely to coordinate insolvency proceedings in different countries. A new chapter would address the issue of insolvency of a firm belonging to a group of companies, enabling a coordinated restructuring plan for the entire group. Finally, the proposal would abolish the requirement that secondary proceedings must also be winding-up proceedings. The proposal does not envisage harmonisation of national insolvency procedures, but in an accompanying communication the Commission announced that it will analyse the impact of divergences between national insolvency laws.

In May 2013, the EP's Impact Assessment Unit positively evaluated the Commission's impact assessment. In December 2013, the Committee on Legal Affairs adopted its first-reading report, welcoming the proposal. A number of amendments were tabled, aimed at removing ambiguities and aligning the text with other EU legal acts, as well as enhancing the coordination of insolvency proceedings in a group of companies by providing for special "group coordination proceedings"[4].

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[3] *Efforts to make resolving insolvency easier in Europe are proceeding slowly*, http://www.economist.com/news/business-and-finance/21629190-going-bust, accessed November 2014.

[4] *Reform of the EU Insolvency Regulation*, http://epthinktank.eu/2014/02/01/reform-of-the-eu-insolvency-regulation/, accessed November 2014.

The objective of this Recommendation is to ensure that viable enterprises in financial difficulties, wherever they are located in the Union, have access to national insolvency frameworks which enable them to restructure at an early stage with a view to preventing their insolvency, and therefore maximise the total value to creditors, employees, owners and the economy as a whole. The Recommendation also aims at giving honest bankrupt entrepreneurs a second chance across the Union[5].

The Commission Recommendations will help to provide a coherent framework for national insolvency rules, asking Member States to:[6]

1. Facilitate the restructuring of businesses in financial difficulties at an early stage, before starting formal insolvency proceedings, and without lengthy or costly procedures to help limit recourse to liquidation;
2. Allow debtors to restructure their business without needing to formally open court proceedings;
3. Give businesses in financial difficulties the possibility to request a temporary stay of up to four months (renewable up to a maximum of 12 months) to adopt a restructuring plan before creditors can launch enforcement proceedings against them;
4. Facilitate the process for adopting a restructuring plan, keeping in mind the interests of both debtors and creditors, with a view to increasing the chances of rescuing viable businesses;
5. Reduce the negative effects of a bankruptcy on entrepreneurs' future chances of launching a business, in particular by discharging their debts within a maximum of three years.

The change of insolvency proceedings in the European Union had an impact in other member states. As a result, Romania adopted in 2014 a New Insolvency Law (Law no. 85/2014 on insolvency procedure and insolvency prevention).

2. Romanian insolvency law

Law no. 85/2014 on insolvency procedure and insolvency prevention was published in the Official Gazette, Part I, no. 466 of June 25, 2014. According to the New Code of insolvency, the reorganization plan of an insolvent company will last three years and not one year as is specified in GEO. 91/2013, declared unconstitutional. Moreover, it may be made an extension of a year.

The new law mentions that the execution of the reorganization plan may not exceed three years, calculated from the date of plan confirmation. Payment terms contracts - including credit or leasing - can be maintained by the plan, even if they exceed 3 years. These terms can also be extended with the consent of the creditors, if initially were shorter than 3 years. After completion of all obligations of the plan of reorganization and closure, these payments will continue as the resulting contracts[7].

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[5] European Commission, *Commission recommendation of 12.3.2014 on a new approach to business failure and insolvency*, art. 1.

[6] European Commission, *Insolvency: Commission recommends new approach to rescue businesses and give honest entrepreneurs a second chance*, http://europa.eu/rapid/press-release_IP-14-254_en.htm, accessed November 2014.

[7] Rădulescu, T. (2014), *New approaches of insolvency in Romania. Procedural issues*, articles presented at the 2nd edition of the International Conference „Accounting and Auditing Perspectives", Timisoara.

New Insolvency Code establishes that the reorganization plan will include:[8]
1. Categories of claims which are favoured;
2. Treatment of disadvantaged categories of receivables;
3. Whether and to what extent the debtor, economic interest group members, associations, limited partnerships and general partners of limited partnerships won't have responsibility;
4. What compensation will be offered to holders of all categories of claims, compared with the estimated value that could be received by the distribution in bankruptcy; The estimated value is calculated based on an assessment report prepared by an appraiser appointed;
5. The method of payment of receivables.

Modification of the plan of reorganization, including its extension can be made anytime during the reorganization procedure, without being able to exceed a maximum total duration of the performance plan of four years from the confirmation page. The change may be proposed by any of those vocations to propose a plan, whether or not the proposed plan. The vote on amendment of the creditors will be left with debts outstanding at the time of the vote, in the same manner as voting for the reorganization. The changing of the plan will be confirmed by the bankruptcy judge.

Also, it is stated a threshold of 40,000 lei for companies that want to enter insolvency. In other words, the debtor will be able to require insolvency only if the debts exceed 40,000 lei. The threshold is the minimum amount of the claim to be filed for the opening of insolvency procedure. The threshold value is 40,000 lei both for creditors and debtor, including claims made by the liquidator appointed by liquidation procedure stipulated by Law no. 31/1990, republished, with subsequent amendments, for claims, other than those of employees, for these the threshold being of 6 gross average wages / per employee.

In Law no. 85/2006 was imposed a threshold for a request to initiate insolvency only for the creditor[9], while GEO. 91/2013 was instituted this value both for creditor and debtor. Given this, in Law no. 85/2014 were taken provisions from the emergency ordinance declared unconstitutional.

3. New Romanian insolvency law connections with the EU's Directive

As provided even at the end of Law no. 85/2014, it transposes Directive 2001/24 / EC of the European Parliament and of the Council of 4 April 2001 on the reorganization and winding up of credit institutions, published in the EU Official Journal, L series, no. 125 of 5 May 2001.

The New insolvency law abrogates Government Ordinance no. 10/2004 regarding bankruptcy of institutions credit as detailed as follows.

I. Main news regarding credit institutions participating in the insolvency procedure as preferential creditors.

Insolvency Code introduces several changes regarding the rights of creditors who have claims that it has a cause of preference (claims which are accompanied by a privilege, as the

[8] Law no. 85/2014 on insolvency procedure and insolvency prevention, published in the Official Gazette, Part I, no. 466 of June 25, 2014.
[9] Law no. 85/2006 on insolvency procedure, published in the Official Gazette, Part I, no. 359 of April 21 2006, amended and supplemented.

mortgage and / or its similar rights or a lien on the property debtor's assets), which belong mainly to the credit institutions.

These changes are the following:

a) Allocation of money in the accounts of borrowers who were brought as collateral in favor of the credit institution

The Insolvency Code clarifies the existing regime of money in the account of debtor to the initiation of the proceeding and upon which is built a security mortgage (and cash collateral), establishing that they will be distributed on demand to the creditor by the receiver / liquidator lender holding the mortgage securities to cover its outstanding debts, within 5 days of the request of the creditor.

If the amounts for escrow account in case of opposition, they will be transferred to the bank account of the proceedings, after checking, by the bailiff, to fulfill the substantive requirements of the contract.

b) Limitation of privileged creditors

Insolvency Code makes some remarks on the financing granted to the debtor in the period of observation in order to develop current activities. They:

- Enjoy priority to repayment in case of bankruptcy of the debtor;
- Shall ensure, primarily by affecting certain assets or rights which not form the subject of causes of preference, and in the alternative, if no such property or rights available will affect goods already encumbered with the agreement of creditors' beneficiaries of these causes preference.

In the event that such consent of the creditors will not be obtained, the priority at established restitution will decrease the refund scheme established to lenders of causes of preference proportionally in relation to the entire value of the goods forming the subject of such rights or causes of preference.

c) Compensation of claims arising after initiation

Under the new rules, any creditor has the right to oppose the debtor compensation claims arising after the date of initiation. This represents a significant advantage for credit institutions to provide financing to the debtor in insolvency proceedings. The insolvent debtor moneys borrowed by a banking institution after the date of opening insolvency proceedings may be offset by the amounts generated by the current activity of the debtor that collects credit institutions in the debtor accounts.

II. The main news on insolvency / bankruptcy of credit institutions

Insolvency procedure / bankruptcy of credit institutions is currently governed by the Insolvency Code, with some changes to the legal regime already known, as follows:

a) It establishes the obligation to obtain the prior approval of the National Bank of Romania by insolvency practitioners that want assigned to the file;

b) It regulates the binding member of the committee of creditors Deposit Guarantee Fund in the banking system;

c) The liquidator may submit a proposal on the winding through The purchase of assets and assumption of liabilities, only after consultation with the National Bank of Romania;

d) The liquidator shall notify the Competition Council regarding the potential transaction, if the liquidation of assets of the credit institution is through the purchase of assets and assumption of liabilities.

Conclusions

Insolvencies are a fact of life in a dynamic, modern economy. Around half of enterprises survive less than five years, and around 200 000 firms become insolvent in the EU each year. This means that some 600 companies in Europe go bust every day. A quarter of these insolvencies have a cross-border element. And they are on the rise – the number of insolvencies has doubled since the beginning of the crisis and the trend is set to continue in 2015.

Furthermore, evidence suggests that failed entrepreneurs learn from their mistakes and are generally more successful the second time around. Up to 18% of all entrepreneurs who go on to be successful have failed in their first venture.

It is therefore essential to have modern laws and efficient procedures in place to help businesses, which have sufficient economic substance, overcome financial difficulties and entrepreneurs get a "second chance". Yet, insolvency frameworks in many EU countries currently channel viable enterprises in financial difficulties towards liquidation, rather than restructuring. They also present obstacles to giving honest entrepreneurs a second chance after insolvency by establishing long discharge periods.

As we seen in the present article, the European Commission has adopted new recommendations regarding insolvencies across companies in the EU but the implementation of these rules in the member states is still not completed entirely. Comparing the situation of insolvencies in Romania, the new adopted law in 2014 has unified the aspects regarding companies' insolvency with those specific for credit institutions. As positive effects are expected, further modifications are necessary for the Romanian law on insolvency to be consistent with the current EU's recommendations on insolvency.

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