Mapping Preventive Restructuring Frameworks and the EU Directive for the JCOERE Project

Country Report

Romania

Judge Nicoleta Mirela Năstasie[1]
Dr Cristian Drăghici

The Romanian Perspective on Restructuring

The Romanian legislative framework, the Italian framework and the French framework contain common elements. As with Italy's *concordato preventivo* Romania has a similar procedure (described below as a preventive concordat) together with what is described in this report as an ad-hoc mandate which reflects a similar approach to France. These processes were reformed in 2014. It would seem that the preventive concordat reflects many of the elements of the preventive restructuring directive (Preventive Restructuring Directive 1023/2019) but there are changes which will be made to comply with other elements of the Directive, including changes to the stay. However, as described below the concept of division into classes is not dominant in Romanian insolvency law and so cross class cram down is not an issue. There are nevertheless significant and clearly drawn grounds upon which dissenting creditors can raise an objection to a plan. The *concordatul preventiv* is included in Annex A to the EIR Recast.

PART 1: The General Context of Preventive Restructuring

Function and Aims of Insolvency and Rescue

Like many EU Member States, Romania was greatly influenced by the economic crisis of the mid to late 2000s, which in turn influenced the development of more recent insolvency, corporate rescue and restructuring procedures. The preventive concordat and the ad-hoc mandate provided under Law no. 381/2009 had the aim of providing a buffer against the wave of insolvencies for companies that had not yet reached the stage of 'formal insolvency'. These early reforms, however, were not as effective as hoped. Once Law no. 381/2009 came into force, it was thought that the number of insolvency claims would be drastically reduced for a period of at least 6 months. Unfortunately, the impact of the concordat was minimal, as debtors preferred to file for insolvency and financial institutions were resistant to the procedure, resulting in a slow uptake. Against this backdrop, Romania introduced revised versions of the ad-hoc mandate and preventive concordat procedures in 2014, which seems to have improved the

[1] Judge with the Bucharest Tribunal – VII Section and PhD Researcher at Titu Maiorescu University, Bucharest, Romania.

This report is funded by the European Union's Justice Programme (2014-2020). Project no. 800807

effectiveness of the concordat. While this law was intended to protect the interest of both debtors and creditors, Law no. 85/2014 appears to be more 'creditor friendly'.

Romanian law contains pre-insolvency instruments, which are aimed at obtaining the amicable negotiation of claims through the ad hoc mandate and the conclusion of a preventive concordat. Potential reforms may include continuing the flow of interest for secured creditors; simplifying the approval of the arrangement; and introducing the private creditor test, which also allows public creditors to vote on a concordat plan.[2] The shorter duration of pre-insolvency proceedings and their greater flexibility should encourage the use of pre-insolvency procedures when the business has a temporary and remediable shortfall in liquidity.[3] Pre-insolvency procedures aim to restructure the company through a conventional restructuring of debts, which is achieved through negotiations with creditors. Unfortunately, the debtor's protection against potential enforcement procedures from the non-adherent creditors is less effective. For this reason, most debtors prefer to open insolvency proceedings and propose a reorganisation plan to fully benefit from the protection against enforcement.

Existing Legislative Frameworks

The ad-hoc mandate[4] is a confidential procedure, which is initiated at the request of the debtor in financial difficulty. An ad-hoc agent is then designated by the court and negotiates with creditors to reach an agreement between one or more of them and with the debtor having the overall aim of overcoming the debtor's financial difficulties.

The preventive concordat[5] is a contract between the debtor and creditors that hold at least 75% of accepted and undisputed value of claims, which is then homologated (confirmed) by the syndic judge. It is only opened at the request of the debtor. The debtor proposes a workout and recovery plan with the aim of covering the creditors' claims and the creditors, in turn, support efforts to overcome the financial distress of the debtor. The key effect of the approval of a preventive concordat is that an insolvency procedure cannot be opened against the debtor during that period.

PART II: Specific Substantive Aspects of Preventive Restructuring in Domestic Processes and in the Directive

The Stay of Individual Enforcement Actions

A moratorium does not automatically arise under the ad-hoc mandate; however, in practice creditors are expected to accept a moratorium along with the mandate proposals. Under the preventive concordat, a debtor may request a provisional stay against forced execution.[6] Once the preventive concordat has been approved, a stay of individual enforcement actions arises automatically; its duration is no more than eighteen months.[7] Where a provisional stay is already in place, it is practice not to apply the additional stay under article 29 para 1.

The stay in Romania is connected to the preventive restructuring procedure and will endure for as long as the preventive concordat continues. There are options for discontinuing the concordat – and consequently, the stay if the debtor has committed a severe breach of its obligations or where creditors file a petition to end the procedure. Severe breaches include favouring creditors with unfair prejudice,

[2] "Public creditor" is a term used to define a budgetary creditor. Usually budgetary claims are significant, as typically value and budgetary creditors vote against any kind of pre-insolvency arrangement, restructuring plan or reorganization insolvency plan.
3 '*Codul Insolventei Adnotat'*, The World Bank Group and Romanian Ministry of Justice, in the Program "*Întărirea mecanismului insolvenței în România*" financed by BIRD 2011-2016, 9 <www.just.ro/wp-content/uploads/2016/03/Cod-adnotat-FINAL.docx> accessed 18 November 2019.
[4] Law no 85/2014 on preventing insolvency and insolvency proceedings (The Insolvency Code), arts 10-15.
[5] Law on pre-insolvency and insolvency proceedings no 85/2014, art 5(17).
[6] Law 85/2014, art 25 para 1.
[7] Law 85/2014, art 29-30.

concealing assets and making payments that put the ongoing business at risk.[8] The stay and the procedure are connected and the conditions for termination are quite similar to those set out in article 6(9)(b) of the PRD. It remains to be seen if Romania will have to provide separately for the empowerment of the relevant court to lift the stay without simultaneously terminating the procedure.

The Adoption of Restructuring Plans

Affected parties have the right to vote on a restructuring plan under Romanian law. Specific parties are excluded from voting, namely creditors which, directly or indirectly, control, are controlled or are under joint control with the debtor and the restructuring plan offers them more than what they would receive in case of bankruptcy. The debtor furnishes the list of creditors for the preventive concordat; accordingly, the debtor has flexibility in identifying the creditors that will be involved. Creditors are not separated into classes for the purpose of voting in the preventative restructuring framework, however, there are classes elsewhere within Romanian law, namely within insolvency. The classes in insolvency are secured (receivables with preference rights), salary claims, budget receivables, indispensable claims (receivables belonging to essential suppliers) and other unsecured claims.

As is common within preventive restructuring, the plans in the preventive concordat are adopted on the basis of a majority vote. Adoption occurs when creditors representing at least 75% of the value of the accepted and uncontested claims vote in favour. Judicial examination of the voting process, which has led to the adoption of the concordat, is mandatory; this occurs once the plan is submitted by the administrator and subsequent to its approval by the creditors.[9]

The Confirmation of Restructuring Plans

All restructuring plans are subject to judicial approval and must be confirmed by the syndic judge before they become binding. Confirmation, referred to in Romania as homologation of the preventive concordat by the judge, results in the judge issuing a resolution in the counsel's chamber, after summoning and hearing the concordat administrator. Confirmation is not automatic, in that the syndic judge can refuse to confirm a plan in certain circumstances. These circumstances are:

(i) if the amount of claims challenged and/or disputed in court exceeds 25% of the total amount of claims; and/or

(ii) if the preventive concordat was not approved by the required majority of creditors.[10]

It is worth bearing in mind that the viability of the plan is not analysed by the judge or court, nor are there any provisions in Romanian law that empower a judge to reject a plan on the grounds that it would not have a reasonable prospect of success.

Cross-Class Cram-Down

As creditors are not organised into classes within preventive restructuring and instead the procedure relies on a majority of 75% by claim value to approve and confirm the plan, a cross-class cram-down is not technically possible. Despite the lack of underpinning foundation for a cross-class cram-down, Romania has specific conditions for the confirmation of a plan that could be considered in line with some of the rules contained in the PRD. There are conditions for cramming down creditors in a reorganisation procedure and dissenting creditors can object to the syndic judge if these conditions are not satisfied. For example, dissenting creditors must be given "fair and equitable treatment" under the plan according to article 139(1)(D) of Law 85/2015.

Fair and equitable treatment is achieved if all of the conditions listed below are met:

[8] Law no 85/2014, art 35.
[9] Law no 85/2014, art 28 (1).
[10] Creditors who represent not less than 75% of the amount of accepted and undisputed claims.

(a) no dissenting creditor receives less than they would have received in a liquidation;

(b) no creditor receives more than the total amount of their claim;

(c) no creditor with a lower ranking than the dissenting creditor receives more than it would receive in liquidation and the plan provides the same treatment for each claim within a distinct category, unless the holder of a claim consents to a less favourable treatment for its claim.[11]

Protection of New and Interim Financing

New financing is protected in Romanian pre-insolvency proceedings. In the ad-hoc mandate, the arrangement agreed with the creditors will not be voided by the court or declared fraudulent at a later date, provided that it was (i) made in good faith, (ii) was likely to result in the financial recovery of the debtor, and (iii) was not intended to prejudice certain creditors.[12] The ad-hoc agent is entitled to propose a wide range of debt restructuring measures to creditors and the privileges and guarantees accompanying the debts are contained in the ad-hoc agreement.[13] In order to safeguard the debtor's business, however, the ad-hoc agent can propose limiting the effect of these guarantees and privileges in favour of lenders considered to be essential for restructuring.[14] In the preventive concordat, patrimonial (civil) liability of the directors and other interested parties cannot be incurred if good faith conditions are met.[15]

The draft of the preventive concordat must include a recovery plan, which should specify the means by which the debtor will successfully restructure.[16] If new funds are to be granted during the concordat term, the priority of these amounts upon distribution and after payment of the procedural expenses shall be specified. Interim financing is not regulated in pre-insolvency proceedings; with that said, it is not prohibited either.

PART III: Specific Procedural Aspects of Preventive Restructuring in Domestic Processes and in the Directive

The Threshold of Insolvency

Insolvency is understood as the debtor possessing insufficient cash to pay the undisputed, liquid and enforceable debts, as follows:

(a) The debtor is presumed insolvent when it fails to pay its debt to the creditor within sixty days of the due date;

(b) Insolvency is imminent when the debtor is proven unable to pay its debts when due from the cash available on the due date.[33]

The threshold value is defined as the minimum amount that the claim must meet in order to allow a petition for the opening of insolvency proceedings to be filed.[17]

[11] Law no 85/2014, art 139(2). The ranking of claims / statutory order of priority is set out in art 138(3) of the Law 85/2014.
[12] Law no 85/2014, art 117(3).
[13] These include debt relief, rescheduling or partial reductions, the continuation or termination of ongoing contracts, personnel redundancy or an abstention by the creditor from improving its position vis-à-vis other creditors through guarantees or preferential treatment as well as any other actions it may deem necessary per art 13(3).
[14] Examples of such limitations could include limiting the right of creditors to pursue, preference, interest and penalties.
[15] These are: in the month before payments were ceased, the payments were made in good faith under an arrangement with the creditors, concluded pursuant to out-of-court negotiations for debt restructuring, provided that such arrangement was likely to lead to financial recovery of the debtor and was not intended to prejudice and/or discriminate some creditors.
[16] Law no 85/2014, art 24 (2); the plan must specific:
"…[t]he actions by which the debtor [will] overcome the financial difficulty, such as: increase in the share capital, debt to equity swap, taking a bank loan, bond or similar borrowing, including shareholder loans, creation or termination of branches or operating units, sale of assets, creating causes of privilege; if new funds are to be granted during the concordat term, the priority of these amounts upon distribution, after payment of the procedural expenses shall be specified."
[17] Law no 85/2014, art 5(72).

Romanian law contains a positive definition of insolvency, in that it introduces the criterion of over-indebtedness as a ground for opening the proceeding. It is referred to as *imminent illiquidity* and is established if the debtor will be unable to satisfy the claims when they become due. A threshold for pre-insolvency proceedings, which is applicable to debtors in financial difficulty, also exists.[18] A debtor is undergoing financial difficulty if, despite fulfilling, or having the ability to fulfill, its obligations when due, it has a low short term liquidity ratio and/or a high long term indebtedness ratio, which may adversely affect its ability to fulfill its contractual obligations by means of the resources generated from operations or the resources attracted from its activity.[19]

Debtor in Possession

All Romanian restructuring processes require the appointment of an expert or administrator. The insolvency practitioners do not take over the business, rather the management stays in control; as such, the Romanian pre-insolvency procedures are "debtor in possession" mechanisms. However, the training of these crisis managers leaves much to be desired, as the practitioner generally knows far less about the management of a business than its former management. As such, this is supervision without a sound knowledge of the business. Practically, this has often resulted in loosely managed reorganisations, which ultimately result in formal insolvency.

Rights *in Rem* under the EIR Recast and the PRD

Rights *in rem* (*ius in re*) are understood as rights held by the holder over a 'thing' directly, without the support of any other person. According to Articles 551 – 552 of Romanian Civil Code, the main rights *in rem* are: property rights, rights of superficies, usufruct rights, use rights, habitation rights, servitudes to the charge of the subdued fund, administration rights, and lease rights.[20] The principal right *in rem* that arises in the context of insolvency proceedings is the property right; in insolvency, the property reservation clause (similar to retention of title) is of particular importance because it is normally intended to protect the interest of a creditor by keeping them and their property out of the cumbersome collective recovery procedure of his claim but to directly take possession of the good in which it has property (title).[21] In insolvency proceedings, a creditor that benefits from a property reservation clause will be able to make the claim as a creditor holding a mortgage-like preference, rather than by exercising the prerogatives of the property right on the subject matter of the clause.[22]

Romanian insolvency law provides that the secured creditors have a general priority where the proceeds obtained from the sale of their duly perfected collateral is concerned. This is provided that such proceeds first satisfy tax liabilities, fees, costs, expenses arising from the sale of the assets and claims of secured creditors, which arise after the opening of the insolvency procedure (including the principal, interests and ancillary rights). If the secured creditors are not fully satisfied following the sale of their collateral, the outstanding amounts will be deemed to be unsecured claims. The potential for conflict between rights *in rem* and preventive restructuring frameworks has been identified in Romania, however, there have been few international cases thus far.

[18] Law no 85/2014, art 6.
[19] Law no 85/2015, art 5(27).
[20] G Boroi, CA Anghelescu, Curs de drept civil. Drepturile reale principale, Ed. Hamangiu, Bucuresti, 2013, 9.
[21] According to art. 123 par. (6) of the Law no. 85/2014 on pre-insolvency and insolvency proceedings: "Where the seller of a real estate withholds title in it until the purchase price is paid in full, the sale shall be considered executed by the seller and shall not be subject to the provisions of par (1); the reserve shall be opposable to the judicial administrator/judicial liquidator if the publicity formalities required by the law were performed; the asset which the seller withheld title in joins the debtor's estate and the seller benefits of a cause of privilege according to article 2347 of the Civil Code."
[22] In this context, it is particularly important that any property reservation clause be brought to the attention of the public through the publicity formalities provided by the Romanian law (registration in the land register, registration in the Electronic Archive of Real Guarantees or other special registers) before the commencement of the procedure insolvency, in order to be opposed to other creditors participating in the proceedings.