CONCORDAT PROCEDURE. LEGISLATIVE AND JURISPRUDENTIAL HIGHLIGHTS

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Abstract

Insolvency Code has revived theoreticians' and practitioners' discussions, equally. The voluntary arrangements procedure is considered a legal solution for the prevention and recovery from commercial actors' financial difficulty. The current legal framework establishes a number of imperative conditions for the implementation of this procedure, but in many cases, the application of the current regulation generated different conclusions. In less than half a year, since the entry into force of the law, the practice for each court varied. The paper synthesizes separate opinions and proposes solutions for shaping a more precise legal framework.

Keywords: *financial difficulties, legal framework, insolvency preceedings*

JEL Classification: *K22, K23*

1. Introduction

Commercial activity is regulated by specific rules that stimulate and facilitate commercial transactions. This legal framework implies, as natural and imperative as the existence of rules for the initiation and development of a business enterprise, the rules on the management of commercial failure, so actual in the present time.

The regulation of the comercial activities, which derives from the spirit of the commercial activities, allows greater freedom for its players and traders, but imposes strict obligations for them, due to the importance and necessity of regulating the continued operation of the economic system[2].

In the literature, it was shown that commercial insolvency produces the same devastating effect on the economic environment that a serious disease induces to the human body[3]. In that order, the step of preventing insolvency and, if possible, removing its incidence effects on the commercial activities is at least as important as the insolvency procedure itself. In this context, the regulation of concordat procedure demonstrates practical application and equally raises extensive and interesting discussion for juridical literatures specialist.

2. Concept and regulation

For the Romanian legal system, regulations on the activities of traders in financial difficulties have not novelty. Even when adopting the first statutes of the old Romanian law, there has been preoccupation for this issue, as it included provisions relating to bankruptcy. The Caragea Code and Code Calimah, both from 1817, the law for comerce from 1840, and the Commercial Code of 1887 regulated judicial proceedings for bankruptcy trader who had ceased their commercial debts[4].

With the transition to a market economy, the regulatory framework for the conduct of commercial activity, initially outlined by adopting the Companies Act (Law no. 31/1990) and RAs Act (Law no. 15/1990), was completed in required by the adoption of Law 64/1995 on the judicial reorganization and bankruptcy.

Law 85/2006 introduced into the Romanian legal framework the concept of insolvency, with the premise conclusions of the European Commission report on the progress made by Romania in 2004, in the accession process to the European Union. The above-mentioned normative act has

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[3] Csaba Bela Nasz, *Deschiderea procedurii insolvenței*, CH Beck Publishing House, Bucharest, 2009, p. 2

[4] Stanciu Carpenaru – *Drept comercial român*, ediția a V-a, All Beck Publishing House, Bucharest,, 2004, p. 571

brought many novelties and legislative progress, valuing the French model provided by Law No. 846/2005, which regulates insolvency[5].

In the contemporary European Union regulations[6], the insolvency procedure is considered an option for traders who have failed to proceedings prevention of insolvency, qualified as voluntary agreement to avoid insolvency and called in Italian law *concordato* (commercial insolvency arrangement)[7].

Under the influence of these regulations and in response to financial instability facing the business, Romanian legislature adopted Law no. 319/2009, on the introduction of the insolvency arrangement and ad-hoc mandate. This bill proposes debtors in precarious financial state solution arrangement as a way to conclude, in agreement with creditors, a debt payment rescheduling option. The purpuse of this arrangement is to avoid or at least to postpone the onset of insolvency proceedings. Under this regulation, although in force for almost 5 years, there were no more than 5 companies that have opted for the procedure arrangement[8].

In response to the legal doctrine's proposals for amending the insolvency law, considering the broader process of codification of Romanian legislation and amid financial difficulties faced by the Romanian players on business market, the Romanian legislature considered the modification and optimization of the regulatory framework by adopting the Law no. 85/2014 on insolvency prevention procedures and insolvency. Under this law, the insolvency preceedings arrangement (called concordat) receives exhaustive rules. The previous procedure, too stiff and with serious impediments to implementation, has been substantially amended and the current provision enjoys a high level of interest among traders affected by financial pressure. In less than half a year after its entry into force, 305 concordat cases were registered on the Romanian juridical portal www.just.ro[9].

3. Conditions for starting arrangement procedure

Law prevision describes practical possibility for that debtor whose business is facing a financial crisis and who believes that the situation is temporary and it could be exceeded in this scenario, the law allowes the debtor to ask for the creditors consent to apply the necessary recovery measures, thus avoiding judicial reorganization, cumbersome, difficult and most often r does not lead to the desired result or leads to bankrupcy. Furthermore, the procedure legal impediments are backed by commercial impact of opening of the insolvency proceedings, which is governed by the publicity rules of procedure, with direct repercussions on the position of the debtor towards its business partners, ands its position on the specific market where it conducts activity.

By adopting the Law 85/2014, the legislature noted that the precarious financial situation of the debtor may, in fact, resume to the fact that the debtor is the victim of unfavorable circumstances and it is not a trader who has accumulated debts through bad faith conduct of business. In this case, the law considers that the debtor deserves to be protected against the possibility of creditors to fund its commercial activity by legal enforcement operations of certain, liquid and due debts. If the business is able to recover, then this opportunity should be used for the benefit of the employees and the creditors through the concordat arrangement, which is to be concluded for the equal benefit of all creditors.

In terms of legal status, the concordat arrangement is a contract between the debtor and creditors holding at least three quarters of the value of claims accepted and unchallenged. Under this agreement, the debtor proposes a plan for its activity that proves that it is still capable to pay its creditors. The debtor's creditors agree to support the efforts to overcome the financial difficulties in

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[5] Crina-Mihaela Letea - *Dizolvarea si lichidarea societatilor comerciale*, Hamangiu Publishing House, Bucharest, 2008, p. 317

[6] Council regulation 1346/2000/EC on insolvency proceedings.

[7] Klaus J. Hopt and Eddy Wymeersch, *European Company and Financial Law* – third edition, texts and leading cases, Oxford University Press, 2004, p. 697 et seq.

[8] http://adevarul.ro/economie/stiri-economice/In-romania-insolventa-generalizata-concordatul-preventiv-nu-fost-folosit-decat-maxim-cinci-cazuri-1_5405f6ba0d133766a8ccbb67/index.html, accessed on November 9, 2014.

[9]http://portal.just.ro/SitePages/cautare.aspx?k=concordat&r=sitename%3D%22AQ12ZG9zYXJfdmRvc2FyCHNpdGVuYW1lAQFeASQ%3D%22&v1=%2Dmjmpdosardata&start1=1, accessed on November 9, 2014.

which the business is located, accepting to collect their debts according to the arramgement previsions.

The legal framework in force establishes a set of explicit conditions that must be met cumulatively in order to benefit from the arrangement procedure.

1. The beneficiaries of the procedure may be legal persons that coordinates a commercial enterprise, a firm in financial difficulty without being insolvent.

This provision is expressly inserted in art. 16 of law no. 85/2014 and should be read in conjunction with art. 5 pt. 29 of the law, which defines insolvency as the state of the debtor's assets that are characterized by insufficiency of funds available for the payment of certain, liquid and due debts.

Even that in strictly formal terms, insolvency must be established by the competent court by approving the request for the opening of insolvency procedure, the insolvency is qualified by the framework law in force as a factual situation, and not necessarily as a formal situation. Its nature depends on the existence of the judgment made by the bankruptcy judge on the admission application to initiate the procedure, but its existence is, in fact paralyzing for the concordat procedure.

In practice, if the debtor situation characterizes the financial difficulties, it may attempt to avoid the negative effects of insolvency proceedings by calling for opening the concordat arrangement, although the situation of insolvency is circumscribed. Consequently, the judge must examine, in each case, the particular situation of the person, to assess the ability to pay fair and to eliminate the state of insolvency, determining whether the arrangement procedure is possible or not. Courts will assess all commercial operations they have been presented by the debtor in question, according to the records submitted in support of the application, considering the monthly debt and ability to pay (judicial decision no. 1573 / 10.01.2014, the Court of Iasi, Section II bankruptcy).

2. The arrangement procedure is not possible to be launched for the debtors, which have been convicted for economic crimes or against whom bankruptcy proceedings have already started, or who have received a far earlier period arrangement, etc.

By introducing these exceptions, the Romanian legislature had in mind the protection of the honest debtor who has no intent to defraud creditors or unduly delay the bankruptcy proceedings.
This condition is also met under different circumstances by the courts of the country, some judges requiring the submission of certificates of criminal record, for others the only legal requirement in considering the above condition being the affidavit, possibly with the date and identity certification of the issuer.

3. Creditors who have expressed willingness to support the procedure should sum 75% of the amounts established as certain, liquid and due, on the date of approval of the arrangement.

The procedure involves two stages prior arrangement implementation itself.

First, within 30 days starting the date on which the competent court upheld the debtor, by civil sentence, the opportunity to appeal to the arrangement procedure, the debtor together with the procedure administrator must put up and supply a precise arrangement; the document should detail the following elements[10]:

a) the analytic situation of the asset and the liability of the debtor, certified by a chartered accountant or, if applicable, audited by an auditor authorized by law;

b) the causes of the debtor financial state and financial difficulty and, where appropriate, the measures taken by the debtor to overcome its submission to the arrangement;

c) the projection of financial accounting evolution in the next 24 months

The draft arrangement must include a recovery plan, which requires at least:

a) the reorganization of the debtor, through measures such as: restructuring the management of the debtor, changing functional structure, downsizing or any other measures deemed necessary;

b) how the debtor intends to overcome the state of financial difficulty, such as: increasing the share capital, conversion of debt into shares / shares, bank loan or other types of obligations,

[10] Article 24 of Law no. 85/2014.

including loans of members / shareholders, the establishment or dissolution of subsidiary or workstations, sale of assets, establishment of causes of preference; When providing new funding arrangement, the draft arrangement will provide priority to the distribution of these amounts, after payment of expenses.

As discussed in the foreign legal literature, insolvency procedures prior negotiation between creditors and debtors in financial dificulty should be governed by the principle of reasonableness[11]. Romanian law does not expressly rule this principle, so we consider that the practice role will be to outline a way to respect it in ongoing negotiations for the approval of the arrangement. So, in fact, this principle will be insured, without specific regulation. Reasonableness parties are regarded as being ready to propose principles and standards as fair terms of cooperation and to abide by them willingly, given the assurance that other will likewise do so. The parties have the constructive attribute of being reasonable in this way flows from the idea of them being citizen of a societry viewed as fair system of cooperation.

Creditors must be persuaded to accept the debtor's plan, and admit the fact that they could collect the money on more favorable conditions by signing the arrangement, unless in the even of the bankruptcy procedure.

The second stage of prior arrangement implementing is the stage of the vote itself. By law, the creditors may vote for the concordat arrangement no later than 60 calendar days. If a majority of 75% of the debts is not secure, the procedure cannot move towards project arrangement. The debtor has either to provide financial recovery through its own effort (without the support of the creditors), or (most likely) to follow the insolvency proceedings path, possibly with the reorganization.

We note on this issue that the associates who have credited the company may not vote for the concordat procedure approval, unless the arrangement is envisaged that in the project they receive less than they would receive in their claim against the debtor during the bankruptcy procedure (art. 7 para. 6 of the law). This provision is intended to give preference to other creditors vote.

The law also allows, through the offer of arragment, to reduce budgetary claims, subject to the compulsory private creditor test results presentation. According to art. 5 pt. 71 of the Romanian law, the private creditor test is a comparative analysis of the degree of sufficiency of budgetary claim by reference to a diligent private creditor in proceedings to prevent insolvency or reorganization, compared with a bankruptcy procedure. The analysis is based on an evaluation report, prepared by an authorized ANEVAR professional, designated by the budgetary creditor. The reports will include a comparison of the benefits during concordat procedure and during a bankruptcy payment schedule. This rule is directly related to the issue of state aid, reducing budgetary debts having this connotation, explicitly prohibited by the regulation in the European Union. Thus, it is not considered state aid the situation in which the private creditor test distributions attests that the budgetary creditor will receive during concordat procedure higher income than it would receive during a bankruptcy.

4. The concordat administrator, the person who will supervise the voting procedure of the arrangement, will try to bring the parties to an acceptable compromise and will supervise the execution of the arrangement by the debtor. He is a professional insolvency practitioner, who mediates and controls the execution of the arrangement by the debtor, informs the creditors and draws action to punish for breach of contract.

Concordat administrator is appointed by the court of law, at the request of the debtor, by the conclusion of initiation arrangement. Its power of attorney's limits are prescribed by law no. 85/2014 and are more restrictive than the limits for the insolvency administrator or banckrupcy administrator. From a procedural point of view, the competent court to request the arrangement is the court within whose jurisdiction the debtor has its registered office. Proceedings shall be conducted in council chamber and, in principle, the procedure remains confidential throughout its duration. In fact, however, the public nature of the request to initiate the procedure of arrangement is outlined in the registration and publication of the case object within the Romanian electronic case portal (www.just.ro). Moreover, in the majority of the domestic courts of law, the meetings of the council

[11] Rizwaan Jameel Mokal, *Corporate Insolvency Law – Theory and Application*, Oxford University Press, 2005, p. 8.

chamber are, in fact, public meetings, taking place in the same rooms, with the same rigor and display the same level of participation as in public meetings.

4. The legal effects of the concordat procedure

From the perspective of comparative law, English law arrangement effects manifest themselves differently depending on the debtor acknowledged the possibility to choose between the two possible forms, which are respectively termed a composition and a scheme of arrangement. In the case of a composition, the debtor personally retains, or resumes, control of his assets and agrees to play a certain sum to his creditors from the process accruing to him. A scheme of arrangement on the other hand involves the debtorss making over his assets to a trustee who thereafter administers them in accordance with the terms of scheme. In both cases, the proposal must undergo a preliminary scrutiny by a qualified insolvency practitioner, who must report to the court stating whether in his opinion the proposal should be carried forward and submitted to a meeting of the debtor's creditors for possible approval[12].

The Romanian law, starting with the date of approval of the application for a concordat procedure, suspends any individual prosecution against the debtor and suspends the prescription of the right to request the enforcement of claims against the debtor and the flow of interest, penalties and any other related expenses claims.

In addition, during the implementation of the approved arrangement, there cannot be opened any other insolvency proceedings against the debtor, as the creditors are under arrangement. However, if the period of implementation of the approved arrangement, the debtor fails to support current activity and accumulates new debts that meet the conditions for the opening of insolvency proceedings (debts are certain, liquid, due, older than 60 days and higher amount of 10,000 ron), then the arrangement can not paralyze the effect of such a request. Newly installed insolvency has priority over the arrangement approved to the oldest debt.

Any creditor of a judgment may join the arrangement. Application for membership shall be submitted to the concordat administrator, who includes it in the creditors list. We note the utility if this regulation to the possibility of destabilization of the legal situation of the debtor to creditors occurring later. The possibility to join the proceedings is opened to voluntary creditors, who wants to joins the procedure and who would have voted for the arrangement. Otherwise, in the absence of an express and opposite provision, we understand that these creditors are able to file for insolvency and bankruptcy debtor.

5. Termination of the arrangement

The version of termination of a running arrangement procedure for the debtor's activity occurs when the claims included in the arrangement are entirely executed, within a maximum of 24 months. The oldest version of the law provided a deadline of maximum 18 months. If the obligations under the arrangement were not fulfilled, the creditors could vote on a proposal from the conciliator (concordatar administrator, in the current regulation), to extend the arrangement up to 6 months, aaditional to the original duration. Overall, the maximum period for the implementation of the project arrangement was approved throughout the two years.

If the arrangement procedure is successful, at the time limit provided in the contract or before that, if necessary, the administrator will issue an order that will see the realization of the object arrangement. In this case, changes in the claims set out in the arrangement remain final. Of course, the debtor is allowed to take the opportunity to pay off all debts included in the arrangement approved sooner than envisaged by the law, which will lead to the completion of the arrangement before 24 months.

[12] Ian F. Fletcher, *The Law of Insolvency*, London Sweet&Maxwell, 2002, p. 43

According to art. 34 of the law, creditors who voted against the arrangement may request its cancellation, within 15 days after its approval.

If the debtor does a serious breach of the obligations assumed under the arrangement, the creditors may decide to appeal for the resolution of the concordat arrangement. On this aspect, the court of law may deliberate even if it was not included on the agenda. Also, the creditor who holds more than 50% of claims, accepted and unchallenged, may bring this action, under the same conditions. In this sense, actions as favoring one or more lenders at the expense of others, concealment or disposals of assets during the arrangement, payments without consideration or in ruinous condition constitute serious violations of the obligations of the debtor by the arrangement.

I the implementation of the project arrangements by the debtor will not be successful, before the expiry of 24 months, and the administrator considers that it is impossible for reasons beyond the objectives arrangement, that the debtor will succed to finalze the procedure, he may request in the court of law for an order of failure. The judge is entitled to establish that the arrangement and the procedure are terminated and not fulfilled.

6. Conclusions

The Romanian law on preventing insolvency and regulating insolvency procedure (no. 85/2014) establishes a new arrangement procedure (called concordat procedure), which is both elegant and efficient in order to redress the debtors in a financial difficulty. The procedure intends to cover in the highest proportion the accumulated debts, using the shortest possible time. However, the character of the relative novelty of the procedure and the particularities of each specific situation faced by debtors are different. Also, the courts have proved different views on the concept that have led to non-unitary and specific solutions. In this approach, we observe the important role of doctrine to moderate this differences and to improve the application of the regulation in force.

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