LEGAL REGIME APPLICABLE TO THE INSOLVENCY OF THE ADMINISTRATIVE-TERRITORIAL UNITS IN ROMANIA. COMPARATIVE LAW ASPECTS - COLOMBIA, HUNGARY, SOUTH AFRICA, SWITZERLAND AND THE UNITED STATES

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Abstract:
The year 2022 marked the critical point when the shock of a real war between Russia and Ukraine overlapped the almost exhausting struggle with a multidimensional crisis - sanitary, social and economic, generating a truly global crisis in a cascade, unprecedented. At the border between the fight for a post-pendemic recovery and the geopolitical upheavals triggered by the invasion of Ukraine by Russia, the perspective of 2023 remains quite bleak and unpredictable, the regime of "stagflation" already outlining the beginning of a global recession.
The budgetary effort of the states to respond to the crisis triggered by the pandemic has been deepened by the repercussions of the war in Ukraine, which have materialized in the global monetary tightening, the energy crisis in Europe and the persistent inflation, further limiting the ability to respond to the new socio-economic tensions, especially in the middle-income and low-income countries. The macroeconomic result indicators contributed to the downward revision of global economic growth in 2022, with an estimate below 2% similar to previous years. In such a volatile climate, in addition to the deterioration of the social fragility indicator in most countries, we face the fragility of the business "ecosystem", the tensions and financial challenges "rolled over" since 2020 continuing to fuel the upward trend of insolvencies. However, we must admit that these cascading crises were the catalyst for repositioning the image of insolvency in socio-economic culture by prioritizing the instruments of reorganization, recovery and granting a second chance to debtors in financial difficulty.
In this context full of uncertainties, in which we have familiarized ourselves with terms such as insolvency, reorganization, recovery or even bankruptcy, we aim to identify the benefits of establishing such special procedures, but this time we limit ourselves to those applicable to administrative-territorial units and not to the legal regulations applicable to professional traders. The insolvency legal regime applicable to the administrative-territorial units is too little promoted and known at national level, although it complements the existing budgetary rules and procedures and can serve to restructure the debts and the fiscal recovery of the subnational entities, including states and municipalities, bringing to the forefront the need to acknowledge that the high indebtedness of ATUs can lead to a serious danger, can undermine their proper functioning and can affect the provision of essential public services but also the central administration.

After an "overview" of the national regulations on the insolvency of administrative-territorial units, we will "explore" other legal realms to identify different options for the design of insolvency regimes specific to municipalities such as those in Colombia, Hungary, South Africa, Switzerland or the United States.
Keywords: *state of financial normality, state of financial crisis, insolvency of administrative-territorial units, financial recovery plan, comparative law - Colombia, Hungary, South Africa, Switzerland and the United States.*

From pandemic to war – insolvency law in time of crisis. Brief considerations on the insolvency of administrative-territorial units

Covid-19 has emerged in a global economy on an accelerated upward path, offering a tough, costly lesson and imposing a profound transformation and reinvention of society and the economic perspective. While the impact of the Covid pandemic still persists, Russia's invasion of Ukraine has generated new obstacles on the road to global economic recovery, creating an unprecedented socio-economic context, a systemic crisis shaped, on the one hand, by the transformations imposed by the pandemic through the fight for resistance and social and financial restoration, and, on the other hand, by the effects of inflation, the effects of rising energy prices and those of an expected recession, a boomerang effect of wide and considerable financial and economic sanctions imposed on Russia by governments around the world. Thus, the current geopolitical landscape prefaced by Russia's actions has generated tensions in multiple global points of interest, tensions that have overlapped and merged with those generated by the economic and health crisis triggered by the pandemic and fully "unhealed".

According to the September 2022 Report of the Organisation for Economic Cooperation and Development (OECD) [1], the world pays a high price for Russia's war of aggression against Ukraine, in the sense that global GDP stagnated in the second quarter of 2022, and production decreased in G20 economies, with many economies having seen inflation in the first half of 2022 at its highest level since the 1980s. Thus, compared to the OECD forecasts of December 2021, before the outbreak of the Russia-Ukraine war, the global GDP is now projected to be at least $2.8 trillion lower in 2023. Moreover, according to the OECD, inflationary pressures extend beyond food and energy, with businesses throughout the economy "going through" high energy, transport and labour costs, and wider inflationary pressures were already obvious in the United States

at the beginning of 2022, and this is now also obvious in the Euro Area and, to a lesser extent, in Japan.

According to the recent Barometer conducted by Coface, [2] Europe nevertheless remains the target of the hardest prospects, which will face an inevitable recession, resulting in the suspension of unprofitable activities due to energy costs or a rationalization decreed by governments, resulting in reduced production and a decline in GDP. Without sufficient diversification of supply and an orderly reduction in demand, OECD experts believe that all these shocks could reduce the growth of European economies by more than 1¼ percentage points in 2023 compared to the reference value, and increase inflation by more than 1½ percentage point, which would truly unveil the recession of European countries in 2023.

We considered appropriate this short “navigation” through the general, global socio-economic picture, which outlines the reality of the end of the year 2022 and outlines the prospects of 2023, so as to be aware of the current and future economic constraints and challenges, which are obviously reflected in the activity and functioning of the administrative-territorial units, its economic and functional reality being in connection, in interdependence with the business environment, which in turn faces numerous challenges since the beginning of the pandemic, knowing a tortuous and thorny route, imprinted by the “lock-in effect” and uncertainties unprecedented in 2020, by a strong return in 2021 and “sunk” in a systemic crisis in 2022 as a result of the start of the Russia-Ukraine war.

In a more optimistic version, we like to say, rather, that 2020 was the start of an economic and social decline, but also the start of a profound legislative reform, especially regarding the “key” rules aimed at the economy, such as the field of insolvency, which is why we will start from the premise that any crisis becomes an opportunity for a significant reform in society or rather, no crisis should be wasted.

If, regarding the insolvency of the commercial debtors, the law has experienced an alert pace of reform in this period, we cannot say this about the national legislation on the insolvency of administrative-territorial units. As a brief review of the “footprint” that the Covid-19 pandemic has triggered on the legislative “picture” in the field of insolvency of professionals, [3] we mention Law no. 55 of 15 May 2020 on some measures to prevent

and combat the effects of the COVID-19 pandemic,[4] in which the legislator allocated a number of articles, we could even say generously, dedicating Section 8 exclusively to the matter of insolvency, but also Law no. 113/2020 on the approval of GEO no. 88/2018 amending and supplementing certain normative acts in the field of insolvency and other normative acts. [5] Law no. 55/2020 was the start of the legislative reform of the insolvency matter, as a large part of the measures ordered during the alert state were subsequently taken over by Law no. 113/2020, which gave them final character in the Insolvency Code – Law no. 85/2014. Moreover, after a remarkable effort of the specialists and experts from the environments with an impact on insolvency, which started two years ago, we are also glad to see the transposition of Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, debt remission and disqualifications, as well as measures to increase the efficiency of the procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency)[6] by the entry into force of Law no. 216/2022 amending and supplementing Law no. 85/2014 on insolvency prevention procedures and insolvency and other normative acts, [7] thus ensuring modern support for the practice of insolvency.

Unfortunately, we cannot enjoy such an evolution, reform, respectively legislative harmonization and insolvency of administrative-territorial units, as regulated by GEO no. 46/2013 on the financial crisis and the insolvency of administrative-territorial units. It seems to be rather a normative act "covered by dust", left in the shade and "not beleaguered" even at the level of doctrine, especially at the level of central and local administration, proof being that it has not undergone any changes since March 2016, amendment made by Law no. 35/22 March 2016 which also approved GEO no. 46/2013. [8] However, such insolvency mechanisms allow the restoration of the necessary fiscal capacity to cope with acute crises, such as the COVID-19 pandemic, an excessive debt limiting long-term growth and leading to discouragement of the financing of infrastructure and public investments. Moreover, the increase of the debts of an administrative-territorial unit may generate negative externalities for other such administrative-territorial units, but also for the government, by reducing their creditworthiness and increasing the total costs

of loans, the central administration being practically obliged to save the other regions, which may lead to the triggering of unsustainable general fiscal policies.

It is important to start the analysis of our research from a few premises, namely that the legal regime for the insolvency of administrative-territorial units is based on the same reasoning as the insolvency regimes dedicated to natural and legal persons under private law. However, the insolvency of administrative-territorial units is different from the insolvency of professionals on certain aspects. The essential purposes of regulated insolvency proceedings for entrepreneurs are to recover money owed to creditors, to save businesses and to apply a reorganisation plan to viable firms. They may also serve to liquidate assets and facilitate an orderly exit from the market. Instead, the insolvency regimes dedicated to administrative-territorial units, as well as the insolvency regimes applicable to natural persons, focus exclusively on restoring the viability of the subnational entity and on a new beginning.

A subnational entity cannot be dissolved in the same way as a company. Although the main objective of business insolvency regimes is to differentiate between viable and non-viable firms and to balance the rights of debtors with those of creditors, insolvency proceedings concerning administrative-territorial units mainly focus on protecting the core functions of the subnational entity. Consequently, in the restructuring process only a limited number of assets can be seized in order to preserve basic public services. Moreover, the administrative-territorial units face the difficulty to accurately assess their assets and to identify the state of insolvency. Unlike the insolvencies of individuals and companies, the insolvencies of administrative-territorial units cannot be determined often by simply comparing assets and liabilities. In many cases, the assessment of insolvency must involve a complex analysis of current and future cash flows based on a number of assumptions. Account must also be taken of their sovereign powers and the democratic rights of citizens. This limits, for example, the right of creditors to initiate insolvency proceedings and reduces the possibility of third parties intervening in debt restructuring and the adjustment process.

We consider that an insolvency framework well designed for ATUs can have substantial beneficial effects, by imposing fiscal discipline measures and applying an official debt restructuring mechanism, while determining the subnational administrations

and creditors to take reasonable loan and financing decisions (*preventive function*), and in the case of a severe budgetary crisis, to contribute to finding a solution *ex post* (*corrective function*), and more design options for insolvency regimes can be extracted, by reference to the legal frameworks outlined by other states. The way in which the specific characteristics are chosen depends on the objectives to be achieved: the provision of essential public services and the strengthening of fiscal adjustment and consolidation, the discouraging strategic non-compliance by an administrative-territorial unit, the facilitation of debt restructuring, the protection of the contractual rights of creditors and the limitation of interference with subnational sovereignty and constitutional rights.

An insolvency framework facilitates debt restructuring and allows a fresh start. As a comprehensive approach, it is superior to *ad hoc* and often chaotic contractual negotiations and approaches, such as collective action clauses. Thus, an insolvency framework can include all creditors' claims, from those of state employees to bondholders. If designed in a predictable and transparent manner, it creates legal and procedural certainty for all parties involved in the event of a subnational fiscal crisis. Above all, debt restructuring may involve extending the maturity of the debt and reducing the amount of interest and principal payments.

Besides its corrective and preventive function, an insolvency regime also serves as an insurance against the long-term negative effects of determined shocks, such as strong decreases in the level of public services.[9] Also, a debt restructuring, such as rescheduling or even a partial annulment negotiated between debtors and creditors, allows ATUs to recover without being obliged to take unjustified decisions on expenditure reductions and tax increases, the repayment of the debt can be postponed until the economic conditions improve. Moreover, insolvency regimes can increase the transparency of the finances of subnational entities, tax transparency being an integral part of many existing insolvency frameworks, as the submission of the insolvency file requires ATUs to disclose all fiscal and financial information, which is often examined by independent third parties.[10]

"Look" at national regulations - GEO no. 46/2013 on the financial crisis and the insolvency of administrative-territorial units

GEO no. 46/2013 on the financial crisis and the insolvency of administrative-territorial units, approved by Law no. 35/2016, represented and continues to represent a sensitive and controversial regulation, which is, in fact, a necessary application and continuation of Law no. 273/2006 on local public finances. The national doctrine considers that these regulations outline the idea of progressive decentralization, "*achieving a normative framework for the transfer of responsibilities from the central to the local level*". In the current conception, decentralization is the indispensable attribute of democracy and implies the idea of autonomy, through decentralization the public administration becomes more efficient and more operative, while the problems are solved at local level, in conditions of maximum operability.

Government Emergency Ordinance no. 46/2013 refers to the ratio between *the state of financial normality* and *the state of financial crisis*, as well as the *state of insolvency* of an administrative-territorial unit, having as a criterion the excess of the administrative-territorial units of the payment obligations they have committed towards third parties over a certain percentage threshold of the general budget of these territorial divisions of the state.

At a first contact with these regulations, the vision of GEO no. 46/2013 seems to be in absolute contrast with the provisions of the Insolvency Code, as regulated by *Law no. 85/2014 on insolvency prevention and insolvency procedures*, due to the following specificities: the administrative-territorial unit is the holder of a public property right, which has in its structure two domains, namely the public domain and the private domain, consequently the goods that enters the public domain of the administrative-territorial unit cannot be liquidated considering the inalienable and imperceptible character, the impossibility of the complete liquidation of the patrimony of an administrative-territorial unit and implicitly the non-entry in the classic bankruptcy, budgetary rebalancing shall be achieved exclusively through the liquidation of its private assets. In fact, the essential difference from the classic insolvency of professionals is that the administrative-territorial units can never go bankrupt.

However, it cannot be denied that the provisions of the two legal acts can be mirrored in terms of the remedial philosophy, which is also reflected in the financial recovery plan drawn up at the level of the administrative-territorial unit. Indeed, the state of insolvency of an administrative-territorial unit can be prolonged *sine die*, in the sense that the recovery plan can be modified, extended or even replaced, the state of the administrative-territorial unit oscillating, based on technical and economic criteria and parameters, from the state of crisis to the state of insolvency and vice versa, but these legal benefits which allow a return to normality are of general interest, unlike the private interests which prevail in the case of professional insolvency. For this reason, during the financial recovery procedure, the Chief Authorising Officer is obliged to ensure the efficient and effective functioning of essential public services, the doctrine [14] assimilating this obligation to the principle of continuity of public services applicable under administrative law, essential being those "public services whose cessation would imperil or jeopardise the existence of the local community".

Pursuant to Article 2, letter m) of GEO no.46/2013, approved as subsequently amended and supplemented, "the financial crisis is the state of the patrimony of the administrative-territorial unit characterized by the existence of financial difficulties, by the acute lack of cash availability, which leads to the non-payment of the payment obligations, liquid and payable, for a certain period of time. The financial crisis shall be presumed in one of the following situations:

m1) non-payment of liquid and due payment obligations, older than 90 days and exceeding 15% of the expenses provided in the general budget of the respective administrative-territorial unit, except for those in commercial litigation;

m2) non-payment of the salary rights provided in the local budget of income and expenses or in the budgets of the institutions or public services of local or county interest, as the case may be, for a period of more than 90 days from the due date".

At the same time, according to art. 2, letter r) of GEO no. 46/2013 "insolvency is the state of the patrimony of the administrative-territorial unit characterized by the existence of financial difficulties, by the acute lack of cash availability, which leads to the non-payment of the payment obligations, liquid and payable, for a certain period of time. Insolvency is presumed in one of the following situations:

r1) non-payment of liquid and payable payment obligations, older than 120 days and exceeding 50% of the expenses provided in the general budget of the administrative-territorial unit, without taking into account those in commercial litigation;

r2) non-payment of the salary rights arising from the employment relationship and provided for in the income and expenditure budget, for a period exceeding 120 days from the due date".

From the perspective of the remedy and recovery, we notice that in the situation of the administrative-territorial units this conception extends both in the situation of financial crisis, in which case the main authorizing officer together with the other members of the committee for financial crisis situations shall prepare a financial recovery plan of the administrative-territorial unit, with the approval of the Territorial Court of Auditors, as well as in the case of the insolvency of the administrative-territorial unit, in which case, following the opening of the insolvency procedure, the judicial administrator appointed by the bankruptcy judge shall draw up the insolvency recovery plan, together with the main authorising officer, with the opinion of the General Directorate of County Public Finance or of the General Directorate of Public Finance of the Municipality of Bucharest and of the Territorial Court of Auditors. The insolvency procedure also involves a judicial activity, carried out by the bankruptcy judge, in this respect approaching more closely the insolvency procedure of professionals, unlike the financial recovery procedure triggered by the financial crisis, which involves more the exercise of active public administration or consultative powers, which is why the applicable legal provisions are also corroborated with Law no. 554/2004 on the administrative contentious.

By mirroring the instrument of judicial reorganization/financial recovery with the reorganization/recovery plan, both as an instrument used by the professional and as an instrument used by an administrative-territorial unit, we find the importance given to it by the legislator in the sense of honesty and interest of the beneficiary subject to implement it, given the consequences of not respecting these commitments. On the one hand, we are talking about the legal possibility granted to creditors and the receiver to request the bankruptcy of the debtor in case of non-compliance with the conditions and terms of the reorganization plan, by accumulating new debts, and on the other hand, we are talking about the legal possibility granted to the receiver to request the bankruptcy judge to take

over the duties of the main authorizing officer only if they do not submit to the approval of the deliberative authority the insolvency recovery plan or if the latter authority does not approve, with or without amendments, the proposed plan, within 10 days from the registration. This possibility also raised a sensitive issue of constitutionality, the doctrine considering that the principle of national sovereignty, enshrined in the Romanian Constitution, is violated, in the sense that the receiver is not part of the category of public authorities, is not elected by universal, direct, secret, equal and freely expressed vote, not being designated by electoral mechanisms. We agree with this opinion, taking into account the principle of separation of powers in the state, which is the foundation of democracy, the legislator "slipping" in this direction from the desire to empower the main participants in this procedure, on which depends ultimately the effectiveness of the implementation of such a plan, with the ultimate goal of restoring the financial balance.

Moreover, considering the manner of design, approval, adoption and implementation of a plan for the recovery of the insolvency of an administrative-territorial unit, in the light of the persons and bodies involved, it is considered to be a unilateral administrative act of normative nature. It should also be realised that a budgetary imbalance gives rise to imbalances in all local economic branches and elsewhere. We are talking about the public-private interdependence in economic terms, we are talking about public procurement, we are talking about a "domino" effect of the financial imbalance. Obviously, the creditors of an administrative-territorial unit in insolvency are at a disadvantage, given that, although a recovery plan cannot be conceived for a period of more than 3 years, if it cannot be implemented during this time, the unit will not go into liquidation as in the case of professionals, but a new recovery plan will be drawn up for a maximum of 3 years or for a shorter term.

As we have not proposed an exhaustive presentation of this normative act, we go beyond the theoretical area and we try to make contact with reality, in order to find that at the level of Romania 7 counties were registered in the Insolvency Register. Thus, if we go to the Ministry of Finance website [15], we note that in the initial phase of financial crisis of the administrative-territorial units, the on-line Register concerns Suceava and Gorj counties, while the Register on insolvency situations, which automatically implies a deficit economic state much more advanced than the state of financial crisis as it concerns

debts older than 120 days, representing more than 50% of the general budget or have not paid salaries for more than 120 days from the due date, concerns five counties, namely Vrancea, Tulcea, Satu Mare, Hunedoara and Bacău.

The first locality in Romania on which the opening of insolvency proceedings was ordered is the town of Aninoasa in Hunedoara County, [16] in 2013, when the debts accumulated by this locality, with over 4,000 inhabitants, reached the threshold of 6 million lei. The Romanian Government decided to allocate the amount of 3.7 million lei from the Budget Reserve Fund, an amount that was used according to the Financial Recovery Plan admitted in 2014 by the Hunedoara Court. Other localities followed, namely Nalbant (Tulcea), Ardeoani (Bacău), Călineşti Oaş (Satu Mare), Naruja (Vrancea) and Andreiașu de Jos (Vrancea), for all of which the insolvency procedure was already closed, the last locality for which the insolvency procedure was closed being Călineşti Oaş, in 2020.

It is necessary to emphasize that since 2015 no such insolvency proceedings have been opened for any locality in Romania. Is this law a failure? Does the stigma of insolvency also affect these issues of law, the local authorities being still reluctant to address such legislative instruments, which currently do not enjoy jurisprudence or doctrinal encouragement? However, the deepening of the research and the development of concrete financial recovery strategies in this field becomes of great interest in the current economic context, given that the specialized literature has strictly stopped at the interpretation aspects of the legal text at the time of its appearance, the doctrine in the field being almost non-existent. We believe that an absolutely essential approach becomes the approach of comparative law, which will sediment the feeling of security in such rules, in the idea that the insolvency of administrative-territorial units finds its application in many developed states that have thus managed to rebalance financially and which can become examples of good practices in the field of insolvency.

As a consequence, the local authorities must take advantage of the existence of these insolvency law rules and avoid as far as possible other ways of financial rebalancing, such as resorting to credits from the state budget, respectively from the Treasury, opting for a plan to reduce the debts according to GEO no. 46/2013. By implementing such a financial recovery plan, as complex as the one regulated by Law no.

85/2014, the capitalization of the assets is used, the reduction by negotiation of the debts, the concession, the lease, the sale of the goods from the private property of the administrative-territorial unit, etc., thus avoiding the indebtedness of the budget permanently by attracting credits from the Treasury, which in reality represent contributions, taxes and duties of the citizens.

Thus, according to art. 5 (4) of GEO no. 46/2013, the financial recovery plan shall comprise:

1. a presentation of the economic and financial situation of the administrative-territorial unit;

2. measures to ensure the provision of essential public services by local public administration authorities during the implementation of the financial recovery plan;

3. measures to improve financial management and control mechanisms necessary to make the provision of essential public services more efficient;

4. measures to increase the degree of collection of own revenues, as well as to generate additional revenues;

5. measures to reduce expenditure;

6. economic - financial and budgetary planning during the financial recovery procedure, which involves:

a) analysis of all budget revenues and expenditures, recommendations for increasing revenues and reducing expenditures, as well as elaboration of corrections to the local budget;

b) projection of income and expenses for the current year and for the next 2 years;

c) restructuring of the leadership, organization and management of the specialized apparatus of the mayor, respectively of the county council, of the public services and institutions of local or county interest, as the case may be;

Of course, the Government also has an essential role to play in balancing local budgets. For example, at the end of 2019, it decided to allocate 475 million lei to save 1,682 municipalities and small towns from insolvency,[17] especially for the payment of salaries, for the settlement of utility bills, social assistance, in the context in which 43 small towns were unable to close the 2019 budget year. Such data represent the real image of the territorial situation, although officially the state of insolvency was not declared in 2019.

The main purpose of an administrative-territorial unit is to return to a financial situation of normality, in the context of these subjects of law, the perspective of recovery being imposed especially, as it concerns the public interest. That is precisely why both procedures regulated by GEO no. 46/2013 are practically reorganization, the state of financial crisis involving a financial recovery plan, and the state of insolvency involving a plan for the recovery of the state of insolvency, the latter being rather identified with the reorganization plan of the professional debtor, in the sense that it cannot be applied for a period longer than three years, with the mention that in case of insolvency of ATU the period cannot be extended.[18]

We mention that, according to art. 7 of GEO no. 46/2013, the financial recovery plan may be amended, when necessary, at the request of the chief authorising officer, where data, information or facts unknown at the time of its approval arise and may hinder the process of financial recovery. The new plan shall be drawn up by the Chief Authorising Officer together with the members of the Financial Crisis Commission and shall be subject to the approval of the deliberative authority. The implementation of the financial recovery plan is mandatory for the authority of the local public administration involved and for the public institutions and services of local or county interest, as the case may be, regardless of the form of financing, which fall under the responsibility of the chief authorizing officer.

Thus, according to Art. 101 of GEO no. 46/2013, at the time of the decision to admit the recovery plan, the activity and structure of the specialized apparatus of the mayor or of the county council, as the case may be, and of the public institutions or services of local or county interest, as the case may be, regardless of the form of financing, are reorganized accordingly, and the claims and rights of creditors and other interested parties are amended accordingly.

Also, in order to increase the value of the patrimony of the administrative-territorial unit, we notice in the content of this normative act, as in the case of Law no. 85/2014, the possibility granted by the legislator to the administrator to propose the unilateral termination or denunciation of any contract, unexpired leases or other long-term contracts, as long as these contracts are not fully executed by all the parties involved and cannot be executed within the recovery plan.

Comparative law aspects - Colombia, Hungary, South Africa, Switzerland and The United States

Only a few countries have established insolvency frameworks for subnational administrations, which have become examples of options for designing and implementing a legal insolvency framework for administrative-territorial units.

The Organisation for Economic Cooperation and Development (OECD) provides us with several studies (2018) [19], including a recent study from 2021, [20] adapted after the one from 2018, studies highlighting the benefits of introducing insolvency frameworks for subnational governments and analyzing existing frameworks in Colombia, Hungary, South Africa, Switzerland and the United States, as well as other frameworks discussed in the literature.

The foundations of such an insolvency procedure were substantiated with the shaping of high budget deficits, with subnational administrations (municipal and regional administrations) accumulating a significant volume of debts, which caused financial problems. For example, in the United States, California has repeatedly experienced severe budget crises between 2008 and 2012. In July 2013, Detroit, whose debt level reached USD 18 billion (USD 26 000 per capita), filed for bankruptcy and recovered after several months. Also in Brazil, the state of Rio de Janeiro declared "a state of financial calamity", in 2016 obtaining an emergency federal transfer in order to host the Olympic Games. [21] In Germany, the deferral states of Bremen and the Saarland were in an imminent budgetary emergency and already in 2011 they were subject to a consolidation programme under the supervision of the so-called Financial Stability Board. [22]

Subnational entities that may be subject to insolvency proceedings may comprise subnational governments as well as subnational agencies, such as public companies or public-private partnerships. In Hungary, South Africa and Switzerland only local governments, municipalities or similar entities are subject to these insolvency laws. American rules define a municipality as "a political subdivision or a public agency or an instrument of a state". This comprehensive definition includes state-sponsored or state-controlled entities that generate revenue through taxes or user charges for the provision of public services (e.g. school districts, hospitals, sanitary districts, public planning districts, bridge authorities).[23]

In our opinion, the insolvency regime of administrative-territorial units is, however, a sensitive subject, as it must certainly take into account the country's particularities, institutional, legal framework and social preferences, in order to achieve an economic-social and administrative balance.

Following the analysis, the OECD has identified an effective and 'balanced' framework model with the following characteristics: the procedure allows the debtor to submit the application that is approved by the court, in order to respect the sovereignty and constitutional rights, allows only a limited set of eligibility criteria by applying the *ultima ratio* principle (discouraging moral hazard) and grants an automatic suspension of the capitalization of assets (facilitating debt restructuring). Also, with regard to debt restructuring, the right of proposal is assigned to the debtor and the right of veto to the court (as regards sovereignty and creditors' rights), a simple majority rule in terms of the number of creditors and a qualified majority rule in terms of debts (facilitating debt restructuring), priority is given to new interim financing (maintaining the financing of loans) and preferential debts over secondary debts (preserving creditors' rights). As regards fiscal adjustment, it provides for the monitoring of subnational fiscal adjustments, for example, on expenditure and taxation, as well as other necessary reforms by the upper-level administration, by accelerating fiscal adjustment while discouraging moral hazard, and provides for sanctions in case of non-compliance.

While experience with existing insolvency proceedings is quite positive, such insolvency frameworks may be difficult to implement in other countries as they may not be compatible with constitutional or sovereign rights or may require major structural and institutional reforms to be effective. Many believe that their introduction may lead to 'contamination' effects at other levels of government or even in the financial markets.

For example, the largest municipal bankruptcy file in the history of the United States is that of the city of Detroit, Michigan. After accumulating debts of more than USD 18 billion (USD 26 000 per capita), Detroit filed for the opening of insolvency proceedings under Chapter 9 in July 2013. By the end of 2014, after 16 months, Detroit had recovered. Under the plan, debts were reduced by $7 billion. Creditors recorded a substantial 80% adjustment in their claims, while pensions were reduced slightly and the fees paid to lawyers, consultants and financial advisors in connection with the bankruptcy generated

a total of over $150 million. Consequently, the insolvency proceedings in Detroit allowed for a fresh start, launching a process of administrative restructuring and attracting new industries and capital. [24]

In May 2017, the American territory in Puerto Rico declared its insolvency, its liabilities totalling USD 122 billion (USD 35,000 per capita and 124% of GDP) consisting of bonds in the amount of USD 74 billion and unfunded pension liabilities in the amount of USD 49 billion.[25] As a result of the unsuccessful debt negotiations, Puerto Rico was subject to the insolvency procedure, as provided for in the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA), the law being heavily criticized in this regard, which raises questions regarding the optimal design of insolvency regimes. [26]

Only a few countries provide regulations dealing with the insolvencies of administrative-territorial units. Many countries, such as Denmark and Australia, have not developed any rules on debt settlement in the event of a subnational fiscal crisis. In Germany and Norway, insolvency proceedings against the assets of the States (Germany), counties and municipalities (Norway) are even prohibited. In these countries, municipalities, states or counties cannot be declared insolvent. Other countries, such as Austria, explicitly allow the enforcement of debt against municipal property, but have no specific rules on how to proceed in the event of insolvency.

A remarkable example is the procedure in Chapter 9 of the United States, which stems from the Municipal Bankruptcy Act of 1938, adopted during the Great Depression and which led to multiple municipal insolvencies. At the time, many municipalities issued debt financing bonds. Unable to pay, they faced withholding in the debt negotiations. As a consequence, the primary purpose of the Act was to address this issue of collective action arising in debt negotiations. [27]

Switzerland has experienced only one case of insolvency. At the end of 1998, after accumulating CHF 346 million in debts due to wrong investment decisions, the Swiss municipality of Leukerbad became insolvent and was placed under forced administration. The municipal government, as well as certain creditors, sued the Canton of Valais (Wallis) for failing to fulfil its supervisory functions. In 2003, the Federal Supreme Court rejected the claims and ruled that the law did not provide for cantonal liability for the municipality's

obligations. Consequently, the creditors accepted a debt relief of 78% of their claims and the Canton of Valais offered a guarantee of CHF 30 million. Each year Leukerbad has to repay CHF 1,3 million, so within a decade the outstanding debt has been reduced significantly to CHF 13 million at the end of 2013. In addition to the rehabilitation of Leukerbad, the application of insolvency proceedings has generated additional positive effects, such as the creation of reforms of accounting standards at municipal and cantonal level, the establishment of policies to restore the capital market, the cantons being granted exemption from the support of municipalities in serious financial difficulties.[28]

The need to regulate insolvency in Hungary, Colombia and South Africa is attributed to systemic and institutional changes. In Hungary, regulations for local governments came into force in 1990, allowing unregulated subnational loans and leading to significant increases in public spending. With the macroeconomic recession in the mid-1990s, many local governments were in serious financial difficulty and received central government subsidies to stay afloat. The Hungarian Municipal Debt Adjustment Act was adopted in 1996 and the purpose of the insolvency regime was to limit the moral hazard arising from the rescue precedents and thus to restore local fiscal discipline. [29]

Colombia underwent a rapid process of decentralisation, which began in the 1970s and accelerated in 1991. SNGs were given more responsibility for the provision of public services and relied on increased transfers by the central government. This has led to the lack of decentralization and the lack of interest of the administrative – territorial units to generate their own resources. The rise in debt levels prompted the Colombian government to pass several laws aimed at overcoming institutional weaknesses and discouraging excessive spending and borrowing. One of these measures is the provision of a debt restructuring mechanism defined in Law 550/1999 and supplemented by Law 617/2000. [30]

In South Africa, after the fall of apartheid, municipalities experienced key changes, with the central government guarantee of local debt being abolished and the municipal boundaries “redrawn”, combining the black-and-white, poor and wealthy urban communities. Extensive intergovernmental grants were also awarded to limit the need for borrowing. South Africa’s motivation behind the Municipal Financial Management Act

2003 was to provide a comprehensive framework for SNGs with regard to municipal financing and the loan. [31]

Three different types of insolvency frameworks can be distinguished, depending on the role of courts, higher-level administrations or other authorities in the proceedings.[32]

Judicial procedure, in which the court has a wide decision-making authority throughout the insolvency process. For example, in Hungary, the court decides whether a municipality is eligible for insolvency filing, gives its consent to the crisis budget and appoints a trustee who directs and oversees the bankruptcy and reorganization process.

Administrative procedure, in which the upper-level administrations establish the bankruptcy status, carry out the debt restructuring procedure and take control of the subnational finances. For example, an administrative procedure is used in Colombia because the judicial system does not always work well. The bankruptcy proceedings for SNGs are conducted by the Superintendence of Companies (SOC) in cooperation with the Ministry of Finance and Public Debts. Switzerland is also following an administrative procedure, although the courts are also involved in the determination of insolvency, the administration of the creditors' meeting and the establishment of a supervisory board for tax intervention.

In *hybrid insolvency systems*, both the court and the administration are involved in the debt restructuring process, which is also specific to our legal system, as we have analyzed above. For example, in South Africa and the United States, the insolvency court approves the bankruptcy application and the debt distribution system, which sets out how debts will be restructured. The preparation of the restructuring plan and the fiscal adjustment are either left to the Municipality itself (the United States) or to an administrative authority (South Africa, Romania).

In an administrative procedure system, debt payment and fiscal adjustment can be achieved more quickly than in a judicial procedure, especially in countries with an underdeveloped judicial system. The disadvantage of administrative systems compared to judicial systems is that subnational administrations may expect the upper-level administration to provide additional public funding and thus increase the risk of moral hazard. In addition, they may be less immune to political pressure and discretionary

decision-making and tend to be more biased in favour of one or the other than in court proceedings. Hybrid frames could be superior because they combine both systems. As the court takes the final decision on the debt allocation system or the debt adjustment plan, it can be ensured that the outcome is fair and equitable for all parties, assuming that the legal system is efficient.

Insolvency frameworks may be initiated by the debtor, creditors, upper-level governments or other authorities. Filing may be voluntary or mandatory. In most countries, the debtor voluntarily submits the application to the competent court (United States of America, South Africa) or to the competent authority (Switzerland). The argument for requesting the opening of the insolvency procedure by the debtor is emphasized by the fact that they know best the real financial situation and the severity of the indebtedness.

The assessment of SNG's eligibility as well as the management and supervision of the debt restructuring process are also important steps in the insolvency proceedings. Regardless of which institution (e.g. court, trustee, administrative authority, etc.) is involved in the process, it should be provided with the necessary conditions of independence, impartiality and jurisdiction. In all existing frameworks, the insolvency assessment is left to a third party, such as the court (United States of America, Hungary, South Africa or the Department of Tax Affairs (Colombia). In Switzerland, a committee of experts can help to assess the financial situation of the municipality.

In Hungary, South Africa, Colombia and the United States, once the request to open insolvency proceedings is accepted, the court or administrative authority shall appoint a trustee to direct and supervise the debt restructuring process. The United States bankruptcy court or the Colombian Department of Tax Affairs serves to enforce the insolvency rules and settles disputes between the debtor and the creditors. In addition to the existing institutions, creditors and debtors may also establish an *ad hoc* arbitration panel which shall lead the debt restructuring process and settle disputes.

According to the OECD, subnational governments (SNGs) play an important role in public finance in many countries, most of which are responsible for the provision of essential public services (e.g. education, infrastructure maintenance, garbage collection, water supply). At OECD level, in 2014, NGAs accounted for 31% of total government

expenditure and 19% of own revenue (from own and shared taxes and user fees). Their debt is high and has increased in most OECD countries, amounting to 150% on average in 2020. The high indebtedness of the SNGs may be due to institutional weaknesses (e.g. limited taxation capacity) or persistent structural problems where the revenues from own resources and intergovernmental transfers are insufficient to meet the expenditure obligations. Apart from the relatively stable fiscal position of many NGAs, some have been strongly affected by the financial crisis and COVID-19 pandemic.

In order to avoid high borrowing costs, limited access to the capital market and/or stigmatisation of bankruptcy, the debtor may nevertheless follow a prudent fiscal policy. Insolvency frameworks can therefore serve to prevent the insolvency of NGAs ('*preventive function*'). They complement and implement existing measures to protect financial discipline and to strengthen the budgetary constraints of NGAs.

Given the specificities and compromises of each country, we can conclude by stating that there is not an optimal framework for all insolvency cases. The design of an insolvency procedure for subnational administrations and the choice of different characteristics should be fully in line with a country's priorities and the country's cultural, economic, legal, constitutional and social context.

We believe that in order to maintain essential services and to facilitate fiscal adjustment, the insolvency procedure of the administrative-territorial units should provide for a comprehensive definition of assets that cannot be confiscated, sanctions in case of missing adjustments and tax intervention of the upper-level administration. These latter two characteristics may also serve to discourage moral hazard. Beneficial to the debt adjustment facility are features that grant a temporary stay of foreclosure, stipulate a rule imposing a debt restructuring plan and define a clear and detailed order of payments. Creditors' rights are best protected when trigger criteria are narrowly defined, the right of veto is attributed to a neutral third party and a wide range of assets can be seized. Ensuring respect for constitutional rights and sovereignty requires strict eligibility criteria, as well as a limitation on asset attachment and political intervention. Based on these characteristics, the existing legal frameworks set different priorities. For example, Chapter 9 of the US Code places greater emphasis on facilitating debt adjustment, in particular by discouraging the problem of collective action and protecting constitutional rights

compared to other countries, but places less emphasis than other insolvency frameworks (Hungary, South Africa and Switzerland) on protecting public services and promoting fiscal adjustment.

Conclusions

The seriousness of the insolvency of the administrative-territorial units results first of all from the damage to citizens and society in general, the respective city entering into a maze of debts and decline by losing the confidence of potential investors, the migration of current investors to other cities, the loss of jobs, lowering salaries, affecting the provision of essential public services, discouraging the financing of infrastructure and public investments, thus limiting the long-term growth and finally declaring a city "dead", abandoned. At the same time, the effect can occur in a chain, the increase of the debts of a single city can generate negative externalities for other administrative-territorial units, but also for the central administration, by reducing their solvency and increasing the overall borrowing costs. Excessive levels of their debt increase the likelihood that a default on debt will lead to "contagion", thus preventing all levels of government from accessing loans and even threatening overall financial stability, as Argentina experienced, for example. In this context, the central administration will be forced to rescue the other administrative structures, which may trigger an unsustainable fiscal policy.

In the current context, it is also very important to increase the capacity of absorption of European funds by all administrative-territorial units, Romania being able to benefit in the coming years from a large volume of European funds, funds made available by the European Union through NextGenerationEU in order to achieve the targets in terms of reforms and investments to support resilience, preparedness for crisis situations, adaptability and growth potential. Here, too, we consider the implementation of the National Plan for Recovery and Resilience (PNRR),[33] the major objective being to create a unitary framework legal regime, coherent for the central and local public administration, approached in close correlation with the activity of coding stable codes

that will contribute to increasing citizens' confidence in the continuity and sustainability of legal regulations.

All these harmonized actions lead to avoiding the indebtedness of the administrative-territorial units and the use of the legal framework regarding insolvency only as a prevention mechanism and not as a correction mechanism, as we have pointed out in our research from a comparative perspective.

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