# ENACTMENT OF THE EUROPEAN DIRECTIVE 2019/1023 IN ROMANIA. BENEFITS OF THE RESTRUCTURING AGREEMENT PROCEDURE

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**Abstract:**
Since 2011, a series of measures have been adopted by European Union, with the initial purpose to harmonizing of the very specific aspects of substantial law of insolvency, including restructuring, but also regarding the company law. The enforcement of Regulation (EU) 2015/848 on insolvency proceedings aimed solving the conflicts of jurisdiction in cross-border insolvency proceedings and ensuring the recognition of insolvency decisions on the territory of the Union. However, the Regulation did not seek to harmonize the substantial law of insolvency in the Member States.
Even though in some Member States, including our country, the Commission's Recommendation was received as a useful proposal to undertake insolvency reforms (adoption of Law 85/2014 regarding the insolvency and insolvency prevention procedures in Romania), it did not succeed in generating uniform changes in all Member States to facilitate the rescue of companies in financial difficulty and to enable entrepreneurs to benefit from a second chance. The Recommendation did not have the expected effects because its partial implementation, even at the level of countries where real reforms have been made regarding the insolvency law. In this context, this study aims at an analysis of insolvency prevention procedures in our country, reported to the Directive of the European Parliament and of the Council, on preventive restructuring frameworks.
**Keywords**: restructuring frameworks, insolvency, preventive concordat, ad-hoc mandate

## 1. General context of preventive restructuring. Function and objectives of insolvency and recovery measures

Like many Member States, Romania was influenced by the economic crisis of 2009, which in turn influenced the modern development of insolvency, corporate rescue and restructuring procedures.

The Preventive Concordat and the Ad-hoc Mandate Law no. 381/2009 [1], had the aim of providing a buffer against the wave of insolvencies, which were not necessarily

justified by a real cessation of payments. These early reforms, however, were not as effective as hoped. After the Preventive Concordat and the Ad-hoc Mandate Law no. 381/2009 came into force, it was foreseeable that the insolvency claims would be drastically reduced for a period of at least 6 months afterward. Unfortunately, the effectiveness of the concordat was minimal. The debtors preferred to file for insolvency and financial institutions were resistant to the procedure, resulting in a slow take-up of the concordat.

Against this background, Romania introduced revised versions of the ad-hoc mandate and preventive concordat procedures in 2014, which seems to have improved the position of the concordat. While this law was intended to protect the interest of both debtors and creditors, the Law No 85/2014 is more creditor friendly.

The law contains concrete pre-insolvency instruments aimed at obtaining the amicable negotiation of claims through the ad hoc mandate and the conclusion of a preventive concordat. 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 project.

The shorter duration of pre-insolvency proceedings and their greater flexibility should encourage the parties to use pre-insolvency procedures when the business has a temporary and repairable shortfall in liquidity [2].

Pre-insolvency procedures aim to restructure the company through a conventional restructuring of debts subject to 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.

In Title I of law no. 85/2014 on insolvency prevention and insolvency procedures, insolvency prevention procedures are regulated, respectively the ad-hoc mandate and the preventive arrangement.

The ad-hoc mandate [3] is a confidential procedure 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 the debtor with the aim of overcoming the debtor's financial difficulties.

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

On 20 June 2019, it was addopted Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132. Member States have two years from publication in the Official Journal of the European Union to implement the new provisions, but in duly justified cases they may request an additional year from the Commission to implement them [4].

The general objectives of the Directive are to contribute to the proper functioning of the internal market, to reduce the most important barriers to the free movement of capital and to the freedom of establishment resulting from differences between Member States in restructuring and insolvency frameworks. and to strengthen the culture of rescuing businesses on the basis of the second chance principle.

## 2. Substantial aspects in the field of preventive restructuring, by reference to the provisions of Directive 1023/2019 of the European Parliament and of the Council of Europe

### The Stay of Individual Enforcement Actions

Directive (EU) 2019/1023 of the European Parliament and of the Council on preventive restructuring frameworks imposes the need to grant a suspension, from the moment the preventive restructuring frameworks are called into question, such a suspension of enforcement having a duration of be reasonable between 4 months and a maximum of 12 months. The reason for granting this suspension lies in accessing the restructuring frameworks as efficiently as possible, before and as a priority, the opening

of insolvency proceedings [6]: m*ember States shall ensure that debtors can benefit from a stay of individual enforcement actions to support the negotiations of a restructuring plan in a preventive restructuring framework*. [7]

A moratorium does not automatically arise under the ad-hoc mandate. Following the appointment of the ad hoc agent by the president of the tribunal, majority creditors should grant the debtor a suspension of individual enforcement of outstanding or short-term claims (postponement of enforcement, judicial or extrajudicial proceedings or insolvency proceedings against the debtor).

In the procedure of the preventive concordat, based on the offer to be agreed, the debtor may request the syndic judge to suspend all individual forced executions, regardless of the object of execution or the quality of the following creditor. The temporary suspension of the individual forced pursuits is maintained until the pronouncement of an executory decision approving the concordat or until the rejection of the offer of concordat by vote by the creditors whose uncontested claims make up the credit table, according to the law.

Also, the provisions of art. 29-30 of Law no. 85/2014 provide for the suspension of individual enforcement actions. According to these provisions, from the date of communication of the decision approving the preventive concordat, the individual proceedings of the signatory creditors against the debtor and the limitation of the right to request the forced execution of their claims against the debtor are suspended. The flow of interest, penalties and any other expenses related to receivables is not suspended from the signatory creditors, unless they expressly express, in writing, their agreement to the contrary, an agreement that will be mentioned in the draft agreement.

The most important effect of the approval of the preventive concordat is that all enforcement procedures are suspended, and during the composition period the insolvency procedure cannot be opened against the debtor. Any creditor who obtains an enforceable title over the debtor during the procedure may file an application to join the preventive concordat or may recover his claim by any other means provided by law.

In the opinion of the practitioners, the temporary suspension of the individual forced execution provided by art. 29 para. (1) of Law no. 85/2014 shall apply only if the provisional suspension has not been previously requested and obtained pursuant to the

provisions of art. 25 para. (1) of the law. Also, the suspension provided by art. 29 para. (1) has the character of *ope legis* and enters into force from the date of communication of the approval decision to the signatory creditors, as opposed to the suspension provided by art. 30 para. (1) which has a judicial character and produces legal effects from the pronouncement.[8]

In the future, legal provisions are needed, relating to certain claims or categories of claims excluded from the scope of the suspension of individual enforcement proceedings, in well-defined circumstances where such exclusion is duly justified and also to avoid abuse of law. Also, the initial and total duration of the suspension of the individual enforcement proceedings and the categories of creditors to which these legal provisions apply will have to find a strict regulation.

**The role of creditors in adopting preventive restructuring plans**

The provisions of art. 9 paragraph 2 of the Directive imposes on the Member States the obligation to ensure that the affected parties, with certain exceptions provided by art. 9 paragraph 3, have the right to vote on the adoption of a restructuring plan.

In the insolvency prevention procedures provided by Law no. 85/2014, the creditors have the right to vote on the reorganization / restructuring plan, either directly or indirectly.

The list of creditors, in the procedure of the preventive concordat, is elaborated by the administrator, together with the debtor. Legislation offers the debtor a great freedom to identify the creditors to whom he wants to propose a restructuring plan.

Creditors have the right to vote on the preventive composition offer, with any amendments resulting from the negotiations, and the vote is exercised, in principle, by correspondence. Certain creditors are restricted from the right to vote, respectively creditors who, directly or indirectly, control, are controlled or are under common control with the debtor. This category of creditors can vote on the composition agreement only if it grants them less than it would receive in the event of bankruptcy.

In insolvency prevention proceedings, creditors are not separated into categories and do not have priority rank for the purpose of exercising the vote. The preventive

concordat is approved with the vote of the creditors which represents at least 75% of the value of the accepted and uncontested claims.

All legal provisions governing the categories of creditors are set out in the chapter on judicial reorganization, which is part of the insolvency proceedings. These provisions should be extended in future to insolvency prevention proceedings so that national law complies with the provisions of the Directive, in order to ensure fair treatment for all creditors of the same rank, to respect the decision of the majority, while allowing other creditors to obtain payments equal to or greater than what he would receive in the event of bankruptcy.

**Debtor in Possession**

The Directive requires Member States to ensure that debtors who resort to preventive restructuring proceedings retain full, or at least partial, control over their assets and their day-to-day business.

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.

In the ad-hoc mandate procedure, the ad-hoc agent, chosen from among the insolvency practitioners, fulfills the role of a mediator between the debtor and one or more creditors, in order to overcome the state of financial difficulty.

In the preventive concordat, the concordat administrator has the role of supporting the debtor, elaborating together with him the preventive arrangement offer.

Doctrine [9], sayd that almost unanimously, the judicial administrator knows much less about the management of a concrete business than the former governing bodies, so that the alleged supervision of the insolvency practitioner turns into a formal verification of the debtor's documents. carried out during the observation period, without real business advice.

The appointment of an insolvency practitioner by a judicial authority should not be mandatory in all insolvency prevention proceedings. Both the ad hoc mandate and the preventive concordat are based on the agreement of the parties, ie the debtor and his

creditors. Being an agreement of wills, which presupposes trust between the parties, means that the very conclusion of such contracts for the amicable settlement of the debtor's dispute with its creditors is a gain in itself for the debtor, since what a debtor lacks in the first place which reaches a state of financial difficulty is the trust of its creditors. By signing such agreements, the debtor regains, at least in part, the lost trust of creditors and business partners.

**Draft law amending and supplementing Law no. 85/2014 on insolvency prevention and insolvency proceedings**

Amendment of Law no. 85/2014 on insolvency prevention and insolvency proceedings by introducing measures to support the restructuring of debtors in difficulty, in order to prevent the entry into insolvency, was not only necessary but also mandatory.

The bill regulates two insolvency prevention procedures, which are in addition to an insolvency treatment procedure: the restructuring agreement, the preventive arrangement (called the restructuring plan, despite the name in Chapter III) and the judicial reorganization. All three of these proceedings are judicial in nature.

The entire chapter II of the Law, regarding the ad-hoc mandate, will be, according to the draft law, repealed.

**3. Compared law aspects**

National legislation on insolvency prevention procedures is largely adapted to the provisions of the Directive and similar to the regulations of other European countries.

In Italy there are three procedures that meet the definition of preventive restructuring: (judicial composition with creditors, the debt restructuring agreement, and the long-term restructuring agreements).

The *concordato preventivo* (judicial composition with creditors) allows a distressed company to avoid opening an insolvency liquidation proceeding by means of an agreement with a majority of its creditors.

The plan is proposed by the debtor, and in some cases by the creditors if they represent at least 10% of the indebtedness, which is known as a competing plan.42 A competing plan can only be submitted in response to a procedure initiated by the debtor.

Competing plans are not admissible if an independent expert certifies that the debtor's proposal ensures the payment of at least 30% of the unsecured claims.43 Upon request by the debtor at court filing, the judicial composition features an automatic stay on enforcement actions; priority for new financing (priority cannot, however, trump secured creditors); termination of executory contracts; intra- and cross-class cram-down; and a stay on recapitalisation obligations. After the approval of the plan by the required majority of creditors, it becomes binding only after judicial confirmation, which will rely on an expert's report certifying that (1) the financial and economic data used in the plan are truthful as to the current situation, and reliable as to the prospects, and (2) that the plan is feasible, and, if implemented, suitable to overcome the crisis.

The *accordo di restrutturazione dei debiti* (debt restructuring agreement) allows for the confirmation of an out-of-court agreement reached by the debtor with at least 60% by value of a company's creditors, supported by an expert's report confirming that the agreement can ensure the full payment of nonconsisting creditors. The key features of this debt restructuring agreement are a temporary stay on enforcement actions, which is automatically granted by the court upon request by the debtor; priority for new financing (not including secured creditors); and a stay on recapitalisation obligations.

The *accordo di ristrutturazione ad efficacia estesa* (debt restructuring agreement binding on dissenting creditors) also allows for the confirmation of an out-of-court agreement. The differentiating feature is that it is also binding on dissenting creditors. The debtor may form one or more classes of creditors on the basis of commonality of interest and an equivalent ranking. All creditors included in a class are bound by effects of the agreement if at least 75% of the total amount of creditors of the relevant class have consented; this results in the remaining 25% of non-consenting creditors being bound. There is no cross-class cram-down provision, meaning that if the 75% threshold is not reached in a certain class, the creditors remain unaffected by the agreement. The key features of this alternative debt restructuring agreement are the temporary stay on enforcement actions at the request of the debtor; an intra-class cram-down; priority for new financing (not over secured creditors, as in the concordato preventivo); and a stay on recapitalisation obligations.

In France, three main preventive restructuring procedures are currently used: the ad hoc mandate, the conciliation procedure and the safeguard procedure.

The French model seems to be one of the most advanced preventive restructuring models in the European Union, although it has continually reformed its legislative frameworks, sometimes without enough time to fully test the procedures in practice. Relative to many other jurisdictions, France has given an early priority to business recue, unless the business is in such a dire situation that liquidation could be the only foreseeable outcome. The French model of insolvency and preventive restructuring has, since the recession of the 1980s, tended to favour the rescue of businesses in order to preserve employment, at times to the detriment of creditors and saving functionally non-viable businesses. Three new insolvency laws were passed during the 1980s, one of which introduced a pre-insolvency process for the first time.55 These laws placed the focus on reorganisation, rather than liquidation with the aim of protecting employment. The focus on employment preservation has changed over the last couple of decades, however, the importance of job preservation is still a clear aim of the French rescue culture.

In the Netherlands, the only preventive restructuring procedure currently available to debtors is the suspension of payments. Besides the suspension of payment, there are no specific formal or pre-insolvency restructuring proceedings available. With that said, it is worth noting that, in practice, the Dutch bankruptcy proceeding is often used to facilitate the restructuring of insolvent debtors.

Germany and Denmark, on the other hand, do not currently offer debtors any preventive restructuring procedure, in the spirit or in accordance with the provisions of the Preventive Restructuring Framework Directive.

While Germany does not yet provide a truly preventive proceeding, their insolvency law does provide for the possibility of proposing a restructuring plan. The Insolvenzordnung of 1999 (the “InsO”) provides a unified insolvency procedure with three paths, one of which is an insolvency plan93 through which there is a possibility to agree a plan with creditors. This can preserve the company as a legal entity by waiving certain residual claims owed to debtors of the company through the plan. The plan also aims for

higher and quicker repayments to debtors than would otherwise be available in a liquidation.

Denmark`s current insolvency framework provides for a restructuring proceeding that aims to overcome insolvency by negotiating a plan, which consists of either a compulsory composition or for the debtor's assets to be sold as a going concern. Functional insolvency is, however, required to utilise this procedure

**Conclusions**

National legislation on insolvency prevention procedures will need to be further adapted and amended in order to comply with the provisions of Directive 2019/1023 of the European Parliament and of the Council on preventive restructuring frameworks.

Although out-of-court debt restructuring agreements are not expressly governed by relevant Romanian legislation, the Insolvency Law and Judicial Practice encourage out-of-court debt restructuring agreements and pre-insolvency proceedings, which aim to safeguard companies through conventional debt restructuring, which is achieved through negotiation with creditors. Unfortunately, the protection of the debtor against potential foreclosure proceedings by non-compliant creditors is less effective. For this reason, most debtors prefer to request the opening of insolvency proceedings and propose a reorganization plan in order to fully benefit from the protection of the law against enforcement.

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