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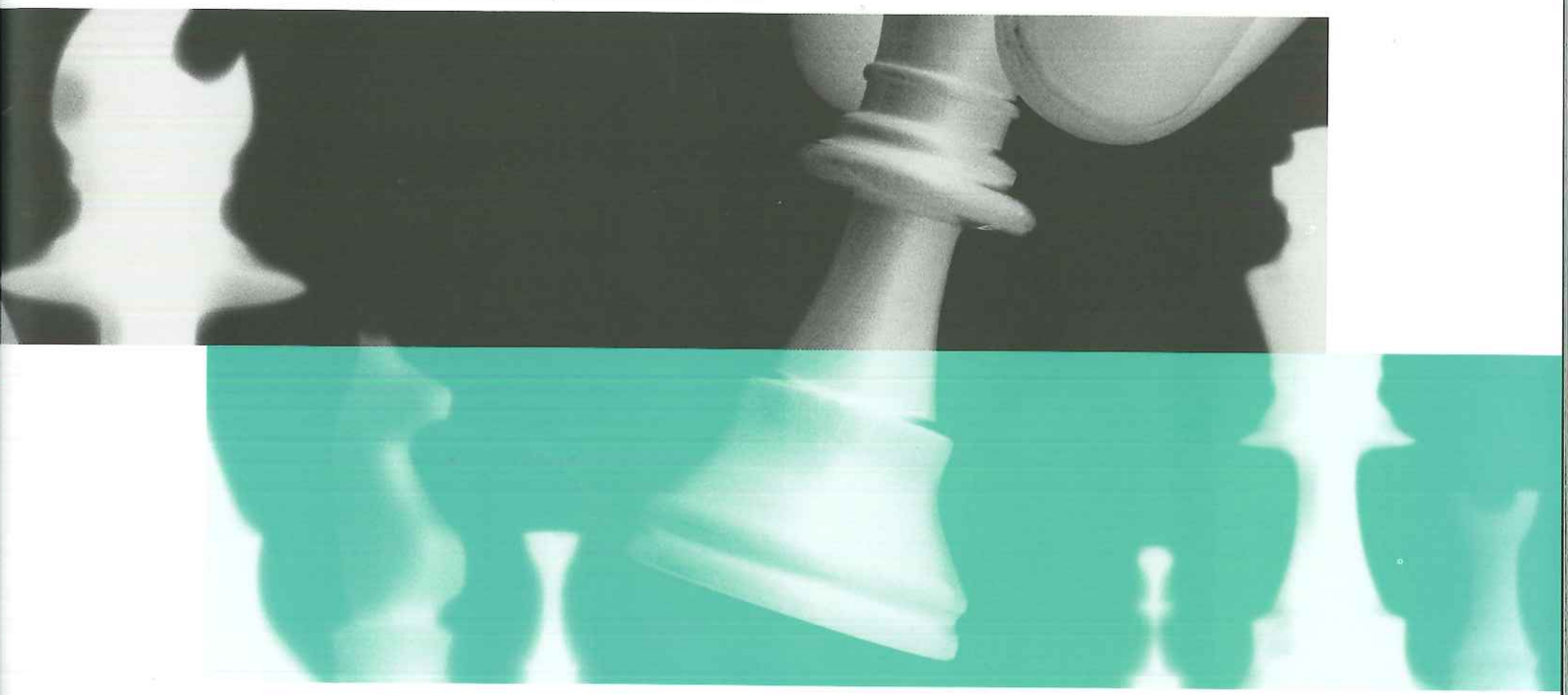

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How to avoid insolvency – ad-hoc mandate and arrangement procedure

KEY POINTS

Advantages of the arrangement procedure:

- initiated solely upon the debtor's request, allowing it to draft the restructuring plan and mechanism of implementation;
- stops the individual claims and the enforcement procedures of the creditors against the debtor and the insolvency procedure, including for non-signatory creditors for the recognised arrangement;
- the debtor does not lose control of its business and the company continues to be managed as usual by its directors under the coordination of the conciliator;
- the role of the syndic judge is minimal;
- a procedure that implies a very low degree of publicity.

Romania has recently taken an important step in filling the existing gap in its legislation regarding debtors' restructuring methods. Aimed at shielding distressed companies from insolvency, the newly introduced ad-hoc mandate and arrangement procedure are now available to debtors. While the ad-hoc mandate does not bring significant advantages, the arrangement procedure permits the debtor to agree with the majority of its creditors upon the repayment, protecting it against enforcement and insolvency and, provided that certain conditions are fulfilled, the arrangement procedure may also bind the creditors who did not vote in favor of the restructuring plan.

INTRODUCTION

At the beginning of 2010, Law no 381/2009 regarding the arrangement procedure and the ad-hoc mandate (the 'Law') was implemented, thus filling a gap existing in Romanian regulations with respect to the European Union countries and importing from the Western practices the *pre-restructuring agreements ('standstill agreements')*.

The procedures proposed by the Law are aimed at preventing the insolvency of debtors, especially considering the significantly increased number of such requests filed in 2009. Practice proved that once the insolvency procedure is commenced, the chances for a judicial reorganisation procedure to be effective are very small, as an enterprise's credibility is dramatically affected. The newly introduced ad-hoc mandate is an extra-judicial, ultra-confidential procedure, while the arrangement procedure hardly involves any court action and is mostly confidential. Neither procedure bears the brand of insolvency.

Last year we also witnessed an increased number of companies negotiating their debts with the creditors and drafting restructuring plans. In this context, the Law is an important step as, until now, even if a debtor reached an agreement with ten of its creditors, for example, the lack of a similar agreement with only one creditor could lead to the commencement of the insolvency procedure.

BENEFICIARIES OF THE NEW PROCEDURES

The Law applies to companies which encounter financial difficulties but are not yet insolvent. The Law defines the debtor as the company which is currently able to pay its debts but is confronted with declining finances and poor management.

Even if the Law applies to all debtors complying with the financial difficulty criteria, the main target are the medium and large enterprises, as their disappearance as a result of bankruptcy would have unfavorable consequences for the entire social and economic background, beginning with the employees losing their jobs, the state losing a taxpayer and bearing the effects of unemployment, the suppliers, etc.

There are certain categories of debtors which do not benefit from the arrangement procedure, especially categories which tried similar procedures in the past or were convicted for economic offences (eg debtors against which an insolvency procedure was initiated five years prior to the arrangement procedure offer; debtors and/or their shareholders/directors convicted for committing economic offences; members of the managing and/or supervisory bodies of the debtor responsible in accordance with the insolvency law for the insolvency status of the debtor).

THE AD-HOC MANDATE

The ad-hoc mandate is a confidential procedure whereby an ad-hoc conciliator, designated by the court, negotiates with the creditors in view of reaching an agreement with one or all of them, intended to overcome the financial difficulty that the company is facing at that time. The procedure of the ad-hoc mandate may solely be commenced by the debtor, by means of a petition addressed to the court, in which the debtor also proposes an ad-hoc conciliator from among the authorised insolvency practitioners. The commencement of the procedure is decided by the court in the presence of the debtor and the conciliator. Within 90 days the appointed conciliator shall seek to enter into agreements with the creditors and, to that effect, may propose debt cancellation, rescheduling or partial discounts, measures with respect to the agreements concluded by the debtor, measures regarding its employees, etc. However, one should consider that although the

conciliator nominated by the debtor and ultimately appointed by the court has as main objective the negotiations with the creditors, he/she does not have any formal power and his/her actions will not bind the creditors without their consent.

The appointment of an ad-hoc conciliator will not suspend the enforcement procedures, will not affect the accrual of interest and will not prevent the creditors from initiating the insolvency procedure against the debtor, provided, of course, that the conditions for such procedure are met, thus making this procedure not specifically useful in practical terms.

THE ARRANGEMENT PROCEDURE

The arrangement procedure is an agreement entered into between the debtor and its creditors, by means of which the debtor proposes a plan of recovery of its business, and the creditors agree to support its efforts to overcome the difficulties that the company is facing.

Request for the arrangement procedure

The procedure is commenced by the debtor by means of a petition filed with the court, whereby the debtor also proposes a conciliator from among the insolvency practitioners. Together with the debtor, the conciliator sets out the list of creditors and the arrangement offer which will be notified to the creditors, filed with the court clerk's office and with the Trade Registry.

The arrangement offer

The arrangement offer includes the arrangement draft and the debtor's statement with respect to its financial difficulty, together with a list of all of its known creditors, including the appealed receivables. A description of the projected financial results for the following six months should also be included.

The arrangement draft must contain:

(i) steps to be taken to change the way in which the debtor conducts its business (including changes in management, operational and employment structures);

(ii) a plan of recovery of the company, including any proposed share capital increases, bank loans, asset disposals, etc;

(iii) the estimated percentage of covering the receivables (which may not be below 50 per cent); and

(iv) the term within which the debts set out in the arrangement must be repaid, which may not exceed 18 months following the date of conclusion of the arrangement. Such term may be extended with an additional period of a maximum of six months. The offer may provide for debt rescheduling, the partial or total release of debt, set-offs and other such measures.

At this stage, the debtor may also request the court to temporarily suspend any enforcement procedures while the arrangement offer is assessed by the creditors and, if approved, the temporary suspension will expire once the arrangement offer is accepted or rejected by the creditors.

Approval of the arrangement by the creditors

Within 30 days following the receipt of the offer, the creditors shall submit their opinion and, if necessary, negotiation sessions shall be organised by the debtor. The creditors should be convinced to approve the recovery plan included in the arrangement offer, in awareness of the fact that they might thus receive the outstanding amounts in conditions that are more advantageous than in the event of bankruptcy.

The creditors will vote either by using fast communication methods or, if necessary, during a conveyed meeting. The arrangement procedure shall be deemed accepted if voted by creditors representing 2/3 of the value of the receivables accepted and not appealed. The votes in favor of the arrangement offer must be unconditional and any qualification of a vote will result in the vote being considered as against the offer. The Law does not grant the secured creditors any special rights or protection in the voting mechanism, consequently, in practice, obtaining the vote of such creditors, especially of the banks, will be more complicated.

Acknowledgement of the arrangement by the judge

After the arrangement offer is approved by the creditors, at the conciliator's request, the arrangement procedure shall be acknowledged by the court. Beginning from the date of communication of the court's ruling, the individual claims and the enforcement procedures against the debtor, as well as the right to request the commencement of the insolvency procedure, shall be rightfully suspended but only with respect to the creditors which are party to the arrangement.

Recognition of the arrangement

In order to render the arrangement opposable to the non-signing creditors as well, either unknown or appealing, the conciliator may demand the recognition of the arrangement. This operation may be performed if the value of the disputed or litigious receivables does not exceed 20 per cent of the total amount of the receivables and if the arrangement has been approved by the creditors holding at least 80 per cent of the total value of the receivables (not just those which have been accepted and are undisputed). The recognition of the arrangement shall suspend all enforcement procedures and shall also prevent the commencement of the insolvency procedure against the debtor.

The debtor will continue to conduct its business as usual, in compliance with the terms of the arrangement under the supervision of the conciliator; however, if the debtor seriously defaults its obligations under the arrangement (eg by favoring one or more creditors, by hiding or transferring assets), the assembly of creditors may decide to ask the court to terminate the arrangement. If such request is approved by the court, the creditors may be entitled to compensation for any damages suffered.

As far as the budgetary creditors are concerned, this procedure is applicable provided that the provisions of state aid are complied with. However, the law is unclear with respect to how tax authorities

Biog box

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should act and how state aid rules should apply in such circumstance and, considering the time regularly necessary for obtaining state aid approvals and the time constraints imposed by the arrangement procedure, it is arguable whether there will be any application of the Law in this aspect.

In the event that the arrangement procedure offer is rejected, a new offer may be submitted after the expiry of a 30-days term.

ADVANTAGES OF THE NEW PROCEDURES

The most important advantage of the arrangement procedure is that it stops the commencement of the insolvency procedure against the debtor in case of recognised arrangement. Also, it permits the debtor to continue to perform day-by-day activities which generate the necessary cash flow for continuing the activities and it stops all delay penalties.

Other advantages of the arrangement procedure and of the ad-hoc mandate include:

- they are initiated solely upon the debtor's request, implementing the debtor's strategy, and not the creditors';
- the debtor does not lose control of its business; moreover, it is assisted by an insolvency practitioner to negotiate and to restructure its business;
- the role of the syndic judge is minimal;
- they are confidential procedures or procedures with a very low degree of publicity.

CONCLUSION

While the ad-hoc mandate has the advantage of being flexible and confidential, however, it has a rather limited impact in practice, since the debtor is able to appoint a consultant to negotiate with the creditors without having to request the court for assistance, the arrangement procedures offers various advantages to the debtor and its creditors.

It is expected that the number of insolvency requests will decrease as a consequence of the Law's coming into force, as both the debtors and the creditors are willing to try such alternatives. Practice will be the real test for the successful implementation of the new alternatives and the willingness of the creditors to agree upon the reorganisation plans of their debtors, especially of the secured creditors which will be placed in line with the other regular creditors. ■