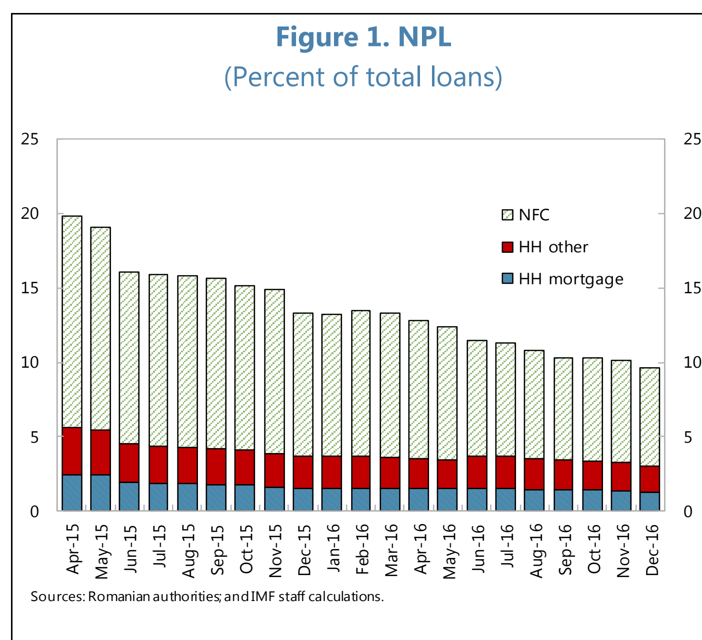
ENHANCING THE IMPACT OF RECENT REFORMS TO THE INSOLVENCY LAWS IN ROMANIA[1]

A. Background

1. Romania overhauled its business insolvency framework in 2014 and adopted a new personal insolvency law in 2015.[2] These reforms aim to modernize business insolvency procedures to better enable the rescue of viable businesses, speed up the liquidation of unviable businesses and recognize the need for a fresh start for over-indebted individuals. The effective implementation of the procedures for resolution of both business and personal insolvency depends on a strong institutional framework, which in the case of the personal insolvency reform is yet to be established.

2. Although nonperforming loans (NPLs) have declined significantly, a strong insolvency framework is important to facilitate efficacious private debt resolution. NPLs have declined to under 10 percent of loans, with about a third of the NPLs in the household segment (Figure 1). Data on the business insolvency law indicates that the pre-insolvency procedures have seen limited use or success, and the judicial reorganization procedure could be strengthened. Further, the insolvency procedure is lengthy and there are often delays which may be attributed in part to overburdened courts and misalignment of the incentives for insolvency professionals. The involvement of public creditors is limited and often not conducive to the reorganization process. Due to delays in setting up the necessary institutional framework, the entry into force of the personal insolvency law has been delayed twice. It is now scheduled to become effective on August 1, 2017, although further delays are likely. Monitoring the impact of reforms through data is difficult as the collection of insolvency data is limited: for instance, no data on size and types of claims is available; and the data available is not regularly published and analyzed.

Figure 1. NPL
(Percent of total loans)



Sources: Romanian authorities; and IMF staff calculations.

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[2] Law No. 85/2014 and Law No. 151/2015

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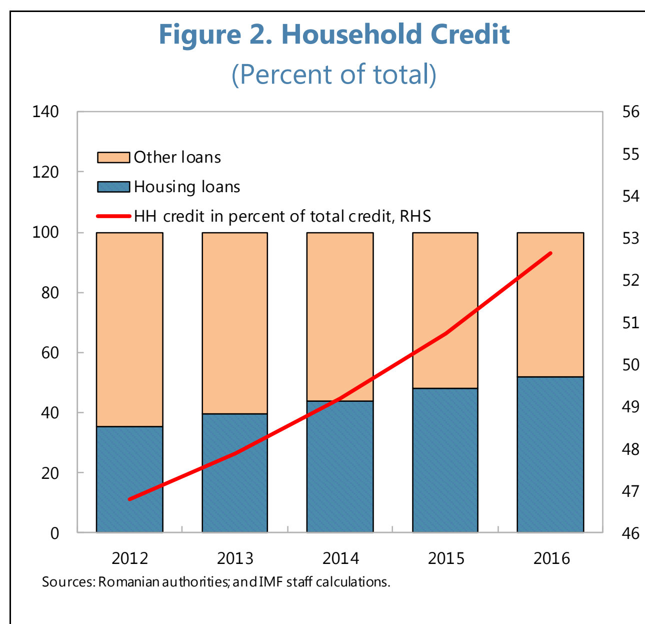
3. This paper takes stock of the status of the insolvency framework in Romania and outlines considerations for the way forward. The first section of this paper analyses the key features of the personal insolvency law, the second section assesses the experience with the business insolvency law, and the third section discusses the adequacy of the methodology for collection of insolvency case data. The final section presents reform recommendations.

B. Personal Insolvency Law

4. Household lending comprises about half of the banks' credit stock. Mortgage lending as a share of credit has been steadily increasing (Figure 2) and more recently, consumer lending has started to accelerate. Given the cyclical position of the economy, interest rates are expected to rise and increase pressure on the payment capacity of debtors. A personal insolvency law may prove useful to both debtors and creditors in addressing individual over-indebtedness.

Figure 2. Household Credit
(Percent of total)



Sources: Romanian authorities; and IMF staff calculations.

5. A well-functioning personal insolvency framework is an important element of a modern debt resolution toolkit. Personal insolvency law should aim to preserve an appropriate balance between maintaining credit discipline and affording good faith debtors a fresh start. It would be a more appropriate tool than ad-hoc solutions that were recently introduced in Romania, such as the mandatory conversion of foreign exchange denominated loans or the retroactive application of the giving in payment law. It would also be timely given the expansion in credit to households and the potential impact of increasing interest rates on the affordability of mortgages.

6. The Law No. 151/2015 on Insolvency of Individuals ("LII") was adopted in mid-2015, but has not yet become effective. Romania's adoption of a personal insolvency law providing over-indebted consumers with a second chance is in keeping with the trend in several Eastern European countries that have adopted personal insolvency laws following the global financial crisis (see Table 1). The LII was adopted without any impact assessment being conducted, an omission that should be remedied. Its implementation has been twice delayed due to the challenges in establishing the new institutional framework required under the law. The authorities expect to start implementation on August 1, 2017.

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Table 1. Personal Insolvency Law Reform in Selected Eastern European Countries						
	Latvia	**Lithuania**	**Poland**	**Slovenia**	**Bulgaria**	**Romania**
Year of reform	2010	2012	2014	2016	N/A Draft Bill introduced in 2015 for protection of over-indebted individuals	2015
Coverage	Consumers only	All natural persons	Consumers only	All natural persons		Consumers only
Procedures available	Debt settlement through a court approved repayment plan follows a liquidation of the debtor's nonexempt assets.	Debt settlement through a court approved repayment plan which could include liquidation of the debtor's nonexempt assets. Fast track" option where a plan and the bankruptcy petition are filed together and the court decides which one to proceed with.	Procedures for debt settlement and liquidation of the nonexempt assets followed by a repayment plan adopted by the court. If the personal situation of the debtor demonstrates that s/he is unable to satisfy any claims under a payment plan, the court may grant an immediate discharge without adopting a payment plan	Liquidation of the debtor's nonexempt assets followed by a court approved payment plan		Debt settlement through a court approved repayment plan and liquidation of the nonexempt assets. Fast track process for debtors with no income and no assets.

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Table 1. Personal Insolvency Law Reform in Selected Eastern European Countries (concluded)

Eligibility	Debtors who are unable to pay overdue debt in an amount exceeding 5,000 euros or debt exceeding 10,000 euro falling due within one year may file.	Debtors with obligations exceeding 25 minimum monthly wages which they cannot meet may file.	Debtor may file along with prima facie evidence of insolvency. Insolvency is presumed if the delay in performing his or her obligation exceeds three months	Debtors obliged to file if the debt exceeds 1000 euro and the debtor is unemployed; or if the debt exceeds three times salary plus income over two months.		Debtor may file if the debt exceeds 15 times the minimum wage.
Primary residence	Sale may be delayed for up to 1 year in certain circumstances	Currently none but special provisions are under consideration	Not excluded from enforcement, however, debtor is awarded an amount from the proceeds of liquidation to pay rent for 12-24 months	Not excluded from enforcement		Not excluded from enforcement, although insolvency professional may suggest how to deal with the residence in the repayment plan
Discharge period	1 to 3.5 years	5 years	3 years (plus 18 months in some cases at court's discretion)	2-5 years (depending on age, family status, health, cause of insolvency, etc)		1-5 years

Source: EC, 2016, Study on a new approach to business failure and insolvency Comparative legal analysis of the Member States' relevant provisions and practices.

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7. The LII establishes two new entities: (i) the Central Insolvency Committee (CIC) which will perform monitoring and coordinating functions and (ii) the Territorial Insolvency Committees (TICs), which will perform quasi-judicial functions and supervise individual cases, in each of Romania's forty-two counties. The design of the LII relies heavily on trained insolvency professionals and the TICs. Districts courts perform only a limited dispute resolution and oversight function, effectively shifting most of the burden away from the judiciary to the TICs

8. The LII provides three procedures for individuals whose debts do not arise from the operation of a business: (i) repayment plan procedure; (ii) judicial liquidation of assets; and (iii) fast track insolvency. Each procedure is time-bound, uses standardized forms, and relies significantly on the use of an insolvency professional. The commencement of any one of the procedures triggers a limited, time-bound stay on individual enforcement action by creditors. The repayment plan procedure is the most flexible and enables the debtor to continue to maintain possession of assets during the procedure and continued ownership over assets at the end of the procedure, to the extent permitted under the repayment plan. The judicial liquidation procedure envisages a liquidation of the debtor's pursuable assets (non-pursuable assets that are exempted from sale include goods for the debtor's personal use, tools of trade, etc.) and continued payments by the debtor for a period thereafter. Each of the three procedures, if successful, affords the debtor with the opportunity for a court ordered release from any residual debts ("discharge"). A court may revoke the debtor's discharge within 3 years if the debtor is found to have committed fraud. (See Box 1 for details).

Box 1. Procedures available under the Insolvency of Individuals ("LII")

The repayment plan procedure under the LII envisages the debtor and a super majority of its creditors agreeing on a repayment plan and confirmation of the plan to bind any holdout creditors. The TIC and the administrator play a key role in the process. The TIC receives applications from debtors, appoints an administrator, issues decisions on whether to accept the plan and monitors the implementation of the plan based on bi-annual reports of the administrator. The administrator assists the debtor with preparation of a plan, notifies all creditors, prepares a table of claims, and facilitates conciliation between the debtor and the creditors. The repayment plan is approved if it is supported by creditors holding 55% of total value of claims and secured creditors holding 30% of the total value of secured claims. If a plan is not approved by the creditors as detailed above, but certain conditions are met (e.g. the administrator finds that the plan is fair and achievable, claims coverage ratio is at least 50% and higher than it would be in liquidation, creditors holding a majority of claims support the plan), the court may confirm the plan over the objections of the holdout creditors. If a plan is not confirmed by the court or the debtor fails to perform under the plan, judicial liquidation proceedings may be commenced (see below). If the repayment plan is successfully completed, the administrator issues a report, the TIC closes the proceedings and the debtor may petition the court for a discharge.

The judicial liquidation procedure under the LII requires settlement of debts through a liquidation of the debtor's pursuable assets, followed by a repayment period. The judicial liquidation process may commence at the debtor's request, or it may follow an unsuccessful repayment

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Box 1. Procedures available under the Insolvency of Individuals ("LII") (concluded)

plan procedure. A court appointed a liquidator takes stock of the debtor's assets, prepares the table of claims (if not prepared in the course of the repayment plan procedure) and liquidates the debtors' pursuable assets. Once the debtor's pursuable assets are sold, the court issues an order closing the proceedings and the TIC takes over the supervision of the case. The TIC assesses the debtor's capacity to pay and reasonable living expenses with the help of the liquidator, and sets the payments to be made by the debtor going forward. The TIC monitors changes in the debtors' finances on a semi-annual basis, and if the debtor acts in good faith (including continuing to share information) and (i) pays at least 50% of the remaining debts in 1 year, or (ii) 40% of the remaining debts in 3 years, or (iii) after 5 years of payments, the court may discharge the debtor.

The fast track insolvency procedure under the LII applies in cases where the debtor has small debts, no income and no assets. The debtor petitions the TIC which conducts due diligence and notifies the court as to its findings. A three-year observation period follows during which the debtor may not run into new arrears, may not take a new loan, and is required to report her financial standing to the TIC on an annual basis before the debtor is discharged. If the debtor's financial situation improves during the observation period (e.g. through new employment, inheritance, etc.), the debtor is required to report the changed circumstances to the TIC and is no longer eligible for a discharge on the basis of the fast track procedure.

9. The LII provides for the collection and dissemination of data on personal insolvency cases by the CIC. It is currently envisaged that the Insolvency Bulletin, which was established in 2006 to serve a summoning and notification function in business insolvency cases and operates under the Ministry of Justice, will have the primary responsibility of collecting personal insolvency data.

10. The schedule for implementing the LII by August 2017 is optimistic. The CIC has been established, and its members have been appointed. However, two critical sets of actions are still pending: (i) actions that the authorities need to take to provide resources to enable the staffing and functioning of the CIC and TICs; and (ii) adoption of secondary legislation and adoption of guidance and rules by the CICs and TICs in their area of competence. Limited progress has been made in both these areas. With regards to the first, a Government Decision to hire personnel for both the CIC and the TICs has been drafted and is under inter-ministerial consideration. In addition, TIC members will be drawn from various Ministries and the Consumer Protection Agencies whose resources may need to be supplemented to allow the hiring of additional personnel to discharge these new functions. Additional logistics such as premises, information technology systems would need to be worked out. Regarding the latter, a Government Decision outlining rules and standards on matters such as reasonable living expenses of the debtor, and treatment of the primary residence has been drafted and is being discussed at the Ministerial level but has yet to be adopted. The LII also envisages a new professional body of qualified and registered administrators and liquidators for personal insolvency cases which will be distinct from the existing body of insolvency administrators dealing

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with business insolvency (together, "insolvency professionals"). The CIC is responsible for setting the standards for the insolvency professionals to be appointed under the LII, which is yet to be done. Additional rules, regulations and guidelines would need to be prepared by the CIC for the smooth functioning of the new system. Debtor awareness materials also need to be developed and disseminated.

11. The LII appears well-designed but its effectiveness in practice will depend largely on its proper implementation. The LII appears to balance the need for credit discipline with affording good faith debtors a fresh start. The relatively streamlined and largely administrative procedures seem well-suited to personal insolvency cases as they provide for less formal and conciliatory processes that take the burden off the court system. The TIC is responsible for debtor counseling (e.g. financial education), legal awareness programs and outreach which if well-implemented will aid individual debtors who lack awareness about their options in case of financial distress. The LII appears to adequately safeguard against moral hazard including through (i) decisions based on full and accurate disclosure of information and the debtor's ability to pay; (ii) limited and clear exemptions of the debtor's assets and income from the insolvency process (see Box 2 for treatment of primary residences); and (iii) an earned discharge from residual debts that follows a period of monitoring and repayment (except in the fast track procedure, where no repayment is expected).

12. Effective implementation of LII requires a sound institutional framework. The secondary regulations (which are yet to be adopted) will be key to the effective implementation of the law. Moreover, an adequate level of supervision and monitoring including by the court would be required to avoid abuse by strategic debtors and for the smooth functioning of the LII. Reliable information systems (e.g. for verification of the debtor's assets based on tax filings) underpin a sound process. The design of the LII envisages an important role for insolvency professionals as both the courts and the TIC rely on the insolvency professional's due diligence, mediation skills and professional opinion. Therefore, a strong cadre of insolvency professionals is crucial to the effective implementation of the LII.

13. Although, there is no international best practice for personal insolvency law against which the LII may be assessed, the LII includes some singular features which bear monitoring. For instance, unlike many countries, the LII provides for different periods before discharge based on the extent to which the debtor has been able to repay its debts and the procedure used (i.e. the period before a discharge could vary from 1 year to 5 years depending on whether the debtor has repaid 50 percent or 40 percent or a lower percentage of its debts). Although not binding, the European Commission Recommendation on a New Approach to Business Failure and Insolvency considers a discharge period of no more than 3 years for entrepreneurs to be reasonable, and this is echoed in the European Commission's Proposal for a Directive on Insolvency, Restructuring, and Second Chance (see Box 3). Some actions by the TIC appear to be mere formalities and could be further streamlined. Once secondary legislation is adopted and following some experience with the functioning of the LII in practice, a comprehensive assessment of the personal insolvency framework could be conducted.

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Box 2. The Debtor's Primary Residence under the LII

Most personal insolvency laws do not provide for any special treatment of an insolvent debtor's primary residence. If there is a mortgage on the home, the secured creditors are normally outside of the scope of the personal insolvency process and accordingly the creditor may enforce and liquidate the collateral in an event of default (Germany, France, Netherlands). Exceptionally, where there is no mortgage on the home, some jurisdictions provide for a limited homestead exemption (e.g. some states in the United States). Table 3 provides a brief snapshot of the treatment of primary residences in Eastern Europe.

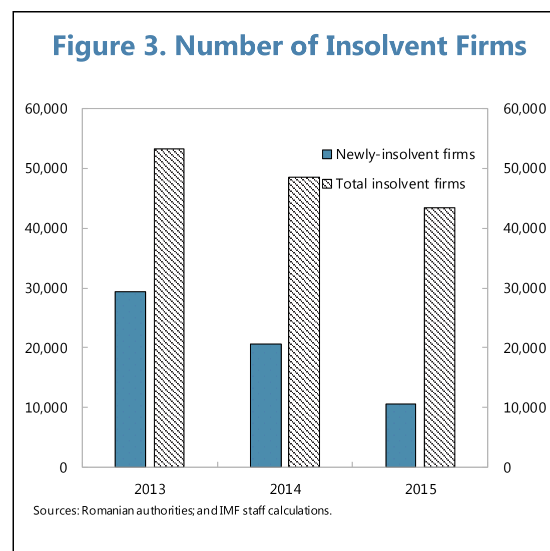
Under the LII, there is no bright line rule for the treatment of the primary residence when the debtor is insolvent. Instead the LII provides that the insolvency professional will work with the debtor to analyze the options with regard to the family residence which could include sale of the family residence, transfer of the property to the banks, or retention of the home by the debtor. The factors that influence the decision include the costs of maintaining the home, the amount of property tax, the amount of rent the debtor would need to pay if the home was sold, installment payments under the mortgage, etc. Unless additional guidance is provided to insolvency professionals, this set of provisions could yield unpredictable results and potentially have a negative impact on both payment culture and banking system.

Additional guidance to insolvency professionals could take the form of a "liquidation test". The personal insolvency laws in some countries enable debtors to keep their primary residences if that alternative is not economically less favorable to the creditors than selling the home (Cyprus, Ireland). In these countries, the debtor may keep its primary residence provided s/he can pay at least as much under a repayment plan as the creditor would have recovered in liquidation. It appears that such guidance is being considered through a Government Decree to be issued shortly.

C. Business Insolvency Law

14. The number of new insolvency petitions has decreased, however the overall amount of debt under insolvency resolution remains high (Figure 3). The improved capacity of firms to service debt due to the economic recovery, as well as write-offs and loan portfolio sales by banks, have resulted in a decline in NPLs. At present, NPLs are highly concentrated in the SME segment (Figure 4). As of September 2016, the firms undergoing insolvency proceedings accounted for 45 percent of banks' NPLs.[3]

Figure 3. Number of Insolvent Firms



Sources: Romanian authorities; and IMF staff calculations.

[3] National Bank of Romania, Financial Stability Report, December 2016.

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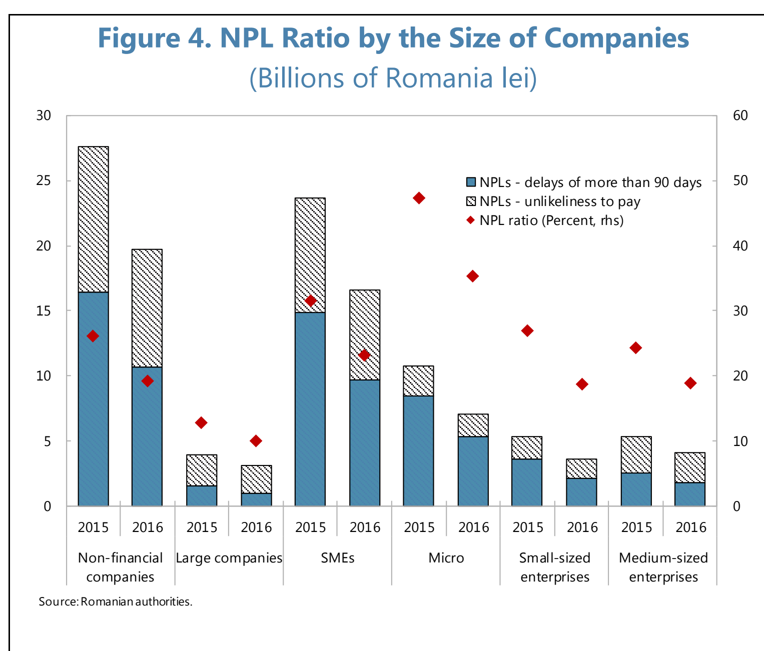
15. Law 85/2016 on Pre-Insolvency and Insolvency Proceedings (the "Code") entered into force in mid-2014. It covers corporates, entrepreneurs and most professionals whose debts exceed a threshold value.[4] Table 2 provides a brief overview of the key features of the Code as compared to other eastern European countries that have pursued reform in recent years. Prior to its adoption, staff conducted a desk review of the draft Code in light of international best practices and cross-country experience, and made recommendations on certain key elements. These included strengthening pre-insolvency procedures, incentivizing post-petition financing, establishing a clear ranking of claims, and improving notice requirements. The authorities accepted several of these suggestions, bringing the Code into closer alignment with international best practices. At the time, staff also emphasized that successful implementation of the Code would require adequate institutional capacity (judges, courts and insolvency professionals), as well as support from other laws and regulations (e.g. tax laws, provisioning rules for banks). Staff recommended that the authorities review the experience with the Code periodically with a view to making changes that could enhance its effectiveness.

16. The Code includes two pre-insolvency procedures, the Ad Hoc Mandate and the Preventative Concordat, both of which have not been much used. The Ad Hoc Mandate is a 90-day confidential procedure whereby the debtor requests the court to appoint an insolvency practitioner to help facilitate discussions between the debtor and its creditors. The Preventative Concordat aims to offer a speedy and cost effective alternative to judicial reorganization. It enables court confirmation of a restructuring plan that is accepted by creditors holding 75 percent of the value of claims, which then binds all holdout creditors. The use and success of both these procedures has been limited possibly due to the high supermajority required for plan approval.[5] The Code also limits the flexibility of the Preventative Concordat procedure by requiring that the recovery plan may only span over a period of 2 years (with a possible extension of 1 year), that 20 percent of the total amount of claims must be repaid in the first year, and that debtors may use the procedure only once every three years.

Figure 4. NPL Ratio by the Size of Companies
(Billions of Romania lei)



Source: Romanian authorities.

[4]Liberal professionals (such as lawyers, doctors, etc.) are excluded from the ambit of the Code. It applies in cases where the cumulative debt exceeds 40,000 Lei (about USD 10,000).

[5]According to data provided by the Insolvency Bulletin, by mid-2016, there were a total of 66 preventive concordat procedures and 3 ad hoc mandate procedures of which agreement was reached in 21 preventive concordants and one ad hoc mandate.

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17. The formal insolvency process commences with a judicial reorganization proceeding, which could be further strengthened. The judicial reorganization proceeding sets out the process by which the debtor and its creditors may agree on a reorganization plan of up to 3 years, facilitated by the judicial administrator and supervised by the court. Once confirmed by the court, a reorganization plan binds all creditors including any hold out creditors. The provisions for voting on a reorganization plan are detailed in the Code.[6] The judicial reorganization procedure is also not frequently used.[7] This is likely because the procedure is too complex, expensive, and lengthy for small businesses (and certain types of small businesses such as individual entrepreneurs and family businesses are not permitted to file for judicial reorganization). Moreover, when it does take place, judicial reorganization is also often unsuccessful.

18. The judicial reorganization procedure has several weaknesses:

- **Creditors do not have sufficiently early input on the appointment of the judicial administrator.** In a voluntary filing, the debtor appoints the interim judicial administrator. The appointment of the interim judicial administrator lasts until the meeting of the creditors committee is called, which could take several months. In the meantime, the interim judicial administrator is in charge of several important tasks (e.g. valuation of assets, preparation of the table of claims), and creditors do not have an adequate level of input. Changing the administrator at a later stage and unwinding past actions causes delay and increases costs.

- **Securing the cooperation of public creditors in debt restructuring is a challenge.** Arrears to public creditors are often a significant percentage of the overall claims against a debtor. Although the participation of budgetary creditors is envisaged in both in the preventative concordat procedure and in the judicial reorganization process, they do not often meaningfully participate. The Code provides that debt restructuring by budgetary creditors is not considered state aid if the private creditors test is met (i.e., it can be shown that such creditors receive more under the plan than they would in liquidation).[8] However, public creditors do not vote in favor of a plan unless they are paid in full. This is for a number of reasons including: (i) an interpretation of the Tax Procedure Code that suggests debts may only be written off if the debtor is dissolved and therefore no debt reduction can be accepted either under the preventative concordat or the

[6]The Code provides for 5 classes of creditors and the plan may be confirmed by the court if it receives the support of (i) the majority of classes (or if there are 2 or 4 classes, then at least half the classes); (ii) at least one class that is impaired; and (iii) a global majority of creditors holding 30% of the value of all claims. Further a plan may not be approved unless dissenting creditors who are impaired receive "fair and equitable treatment", which provides *inter alia* that an impaired creditor should not receive less under the reorganization plan than it would in a liquidation procedure.

[7]Data from the Insolvency Bulletin indicates that since the Code became effective, less than 1000 judicial reorganizations have been filed (out of a total of over 26,000 insolvency cases filed in the same period). As the reorganization procedure itself takes time and the reorganization plans typically span up to three years in Romania, at present there is limited data on the success or failure rate of reorganization plans.

[8]Public creditors in Romania have limited priority in liquidation, i.e. they are paid before all other unsecured creditors but after the expenses and costs of the procedure, the secured creditors, and settling the labor dues. As per the distribution provided under the Code, bondholders are subordinated not just to the tax authorities but also unsecured bank creditors which may negatively impact the development of a corporate bond market in Romania.

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judicial reorganization procedures; (ii) tax authorities have limited capacity or expertise to assess whether the private creditor test is met and state aid is not triggered; (iii) officials are concerned regarding their own personal liability under laws safeguarding against the dissipation of state assets; and (iv) there is a strong perception among the authorities that insolvency filings are often a tactic used by the debtor to delay enforcement of collateral by tax authorities and that such strategic debtor behavior needs to be curtailed. It appears that there is additional confusion caused by conflicting jurisprudence on whether the standstill period under the Code is required to be honored by public creditors in enforcing penalties under tax laws, as well as the interaction between criminal laws and the Code.

- **There are excessive delays.** The design of the law requires that unless the debtor requests immediate liquidation, judicial reorganization is attempted in all cases. As there is no independent assessment of the debtor's viability early in the process, going through the full judicial reorganization procedure can create delays. Additionally, while the Code provides for deadlines for the various steps in a procedure, there are frequently delays due to the overburdened court system. The number of specialized judges working exclusively on insolvency matters is quite limited. Reportedly, judicial administrators often do not have the right incentives to efficiently guide cases through the system (e.g. they often are paid on a monthly fee basis, rather than on a success fee basis).

19. Reorganization of small businesses is not adequately supported under the Code. The vast majority of insolvency petitions filed under the Code have been by small and micro businesses.[9] However, the Code does not appear to facilitate the rescue of such businesses. In particular:

- Unincorporated small businesses (e.g. individual entrepreneurs and family business) are not permitted to use the judicial reorganization proceeding. They are required to request a "simplified liquidation proceeding" which is essentially a quick liquidation procedure. Therefore, unincorporated small businesses have no restructuring options under the insolvency procedures (although they may use the pre-insolvency procedures).

- Where the debtor is an incorporated business and may access the judicial reorganization procedure, the procedure is lengthy, complex and expensive for small businesses. It appears better suited for use by debtors with large debts who have access to interim financing as well as expertise. Moreover, the debt of small business is often backed by personal guarantees and business insolvency may trigger personal insolvency, for which an entirely distinct procedure must be followed.

20. The Code also envisages a liquidation procedure, followed by a discharge for individual entrepreneurs. Liquidation proceedings may be commenced at the debtor's request or

[9]Data from the Insolvency Bulletin indicates that for 2016, of 8392 petitions filed, over 6045 were small and micro enterprises.

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in case the judicial reorganization process fails. In addition, as mentioned above, the Code provides for a simplified liquidation proceeding which is the only alternative for certain categories of debtors (e.g. unincorporated businesses, defunct companies, etc.). Data indicates that over half of all debtors use the simplified liquidation proceeding.[10]

21. Stakeholders have expressed concerns regarding strategic debtor behavior. To afford the debtor an opportunity to restructure and to enable collective action by creditors, the Romanian insolvency law provides for a stay on individual enforcement actions by creditors once the insolvency petition is filed. The stay is temporary and is designed in a manner which is consistent with international best practice. However, reportedly, many debtors file for insolvency solely to delay creditor enforcement actions (including for example, delay the collection actions by tax creditors). This is despite safeguards such as (i) notification of the tax authorities by the debtor before filing for insolvency; (ii) all claims that fall due during the pendency of the stay must be paid in full, failing which the creditors can take action against the debtor.

22. In summary, the business insolvency framework has been strengthened but some challenges remain. The Code has benefitted from the feedback from Fund staff and other IFIs at the early stages of drafting, however, some important shortcomings remain to be addressed. In addition to the weaknesses of the reorganization procedure identified above, the Code does not facilitate the effective restructuring of small businesses as it does not offer a streamlined restructuring procedure. Moreover, the objectives of the Code are not fully supported by regulatory and tax rules. Capacity building and training initiatives aimed at the judiciary could also be strengthened.

[10] Data from the Insolvency Bulletin shows that for 2016, of 8392 cases filed, 5588 filings requested simplified liquidation.

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Table 2. Key Features of Business Insolvency in Selected Eastern European Countries

	Latvia	Poland	Slovenia	Bulgaria	Romania
"Pre-packs"[11]	Yes	Yes	Yes	Not contemplated	Not contemplated
In court rehabilitation procedure	Yes, in-court procedure for development of a rehabilitation plan after filing a petition	Yes, 4 types of reorganization procedures with varying levels of court involvement: Arrangement Approval Proceedings; Accelerated Arrangement Proceedings; Arrangement Proceedings; and Remedial Proceedings	Yes, separate reorganization (compulsory settlement) procedures for medium and large businesses, and small and micro enterprises. In addition, there is a pre-insolvency restructuring proceeding available to medium and large businesses.		Yes, three procedures: ad hoc mandate procedure, preventative concordat, and judicial reorganization which entail varying degrees of court involvement.
Voting majority required	Two-thirds of secured creditors and a simple majority of unsecured creditors. Length of plan is 2 years (plus 2 years extension with consent of creditors)	Class voting, plan should be accepted by each class by a 2/3rds majority of the claims. If not, the plan may still be approved if accepted by 2/3rds of total claims, or the plan ensures that the dissenting classes are no worse off than in liquidation.	No class voting and intricate rules to calculate the voting power of creditors.	Class voting, plan approved by a simple majority of claims. If a creditor holding more than half of claims votes against the plan, it may not be approved, regardless of the outcome of class voting	Court confirmation of the preventative concordat requires – (i) disputed claims do not exceed 25% and (ii) creditors representing 75% of undisputed claims agree. Length of plan may be up to 2 years (plus 1 year extension with consent of creditors).

[11] Expedited procedure for court approval of a rehabilitation plan negotiated between parties before filing of an insolvency petition.

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Table 2. Key Features of Business Insolvency in Selected Eastern European Countries (concluded)

		Most restructuring procedures require that the value of disputed claims does not exceed 15%.			The judicial reorganization procedure follows a system of class voting with a support from a minimum number of classes, and at least 30% a global majority of all claims. Length of plan may not exceed 3 years.
Insolvency practitioner in rehabilitation proceeding	Yes, creditors or court appoint	Yes, creditors or court appoints	Not necessary	Yes, court appoints initially but creditors can replace	Yes, court appoints initially but creditors can replace
Simplified SME procedure	No	No	Yes, simplified compulsory settlement procedure	No	Yes, mandatory liquidation procedure for individual entrepreneurs
Conversion of failed rescue proceeding into bankruptcy	Yes	Yes	Yes	Yes	Yes
Discharge of residual debts of entrepreneurs	Yes	Yes	Yes	No	Yes

Source: EC, 2016, Study on a new approach to business failure and insolvency Comparative legal analysis of the Member States' relevant provisions and practices.

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D. Data Collection and Analysis

23. Reliable data is a key element in assessing the efficiency and effectiveness of the insolvency laws. Findings backed by accurate data offer additional objectivity, credibility and bring accountability to the system. Periodic data measuring the duration and cost of insolvency proceedings and the recovery rates to creditors could assist the authorities in assessing the efficacy of the business insolvency law, and if changes are made to the law, measuring the impact of those changes against a baseline. Additionally, the recent European Commission's Proposal for a Directive on Insolvency, Restructuring, and Second Chance includes a requirement for member states to collect comprehensive statistical data on insolvency cases, focusing on the frequency, length, cost and recovery rates for secured and unsecured creditors, among other relevant data.

24. The purposes for which information is collected determines the type of data collected, the methodology used and the agencies entrusted with the task. Data collection for insolvency cases could focus on (i) general statistics on the number and type of insolvency proceedings with the aim of monitoring economic trends; (ii) NPL resolution and the rate of credit recovery by banks; (iii) measuring the effectiveness and efficiency of the insolvency system (including measuring the impact of reforms against a baseline); and (iv) other purposes (e.g. for budgetary resource allocation for infrastructure and institutional improvements, key performance indicators for courts, etc).

25. In light of the recent reforms to the insolvency system, this paper focuses on data collection that could assist the authorities in measuring the effectiveness and efficiency of the new insolvency system. Such an assessment would consider data collected after a debt resolution process is initiated although the beneficial effects of the system could be far wider (e.g. strengthening credit culture, early action by debtors and creditors to enter into out-of-court workouts, etc.). The analysis of the effectiveness of the insolvency framework thus revolves around the concepts of time taken to complete the proceeding, cost of the proceeding, and the recovery rate. Although outside the scope of this paper, it should be noted that this analysis is impacted not just by the insolvency framework but also the procedures for debt enforcement (e.g. the Civil Procedure Code which sets out the procedures for seizure and sale of assets).

Box 3. European Commission's Proposal for a *Directive on Insolvency, Restructuring, and Second Chance*

The objective of the EC Proposal is to establish certain minimum standards for debt restructuring and insolvency across the European Union, including also special rules for discharge of debt without attempting a full harmonization of insolvency law. The Proposal will follow the usual co-decision procedure, with parallel work at the Council and at the European Parliament. Once a Directive is adopted, member states will have two years to implement it under their national regimes.

The proposal foresees that member states would be required to collect data annually based on a standard methodology, and transmit it to the EC. This data would cover, at minimum, the number of filings for each type of procedure (restructuring, insolvency, second chance), length, outcome of procedures, administrative costs of procedures, recovery rates, and success of such procedures. Member states would also be required to break down this data by size and type of debtors so that the effectiveness of procedures can be objectively assessed. It reads:

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Box 3. European Commission's Proposal for a *Directive on Insolvency, Restructuring, and Second Chance* (concluded)

"1. With a view to arriving at reliable annual statistics, Member States shall collect and aggregate at Member State level data on:

(a) the number of procedures which were initiated, pending and resolved, broken down by:

(i) preventive restructuring procedures,

(ii) insolvency procedures such as liquidation procedures,

(iii) procedures leading to a full discharge of debt for natural persons;

(b) the length of the procedure from initiation to payout, separate by types of procedures (preventive restructuring procedure, insolvency procedure, discharge procedure);

(c) the share of each type of outcome within each restructuring or insolvency procedure, including the number of procedures applied for but not commenced for lack of available funds in the debtor's estate.

(d) the average costs of each procedures awarded by the judicial or administrative authority, in euro;

(e) the recovery rates for secured and unsecured creditors separately, as well as the number of procedures with zero or no more than two percent total recovery rate in respect of each type of procedure referred to in point (a);

(f) the number of debtors subject to procedures referred to in point (a)(i) who within three years from the conclusion of such procedures are subject to either of the procedures referred to in points (a)(i) and (a)(ii);

(g) the number of debtors who, after having undergone a procedure referred to in point (a)(iii) of this paragraph, are subject to another such procedure or another procedure referred to in point (a) of this paragraph.

For the purposes of point (e) of the first subparagraph, recovery rates shall be after costs and anonymised data fields shall show both recovery rate and recovery rate lined to time until recovery.

2. Member States shall break down the statistics referred to in paragraph 1 by:

(a) the size of the debtors involved, by number of workers;

(b) whether debtors are natural or legal persons;

(c) in respect of discharge and where such distinction is made under national law, whether the procedures concern only entrepreneurs or all natural persons.

3. Member States shall compile statistics from the aggregate data referred to in paragraphs 1 and 2 for full calendar years ending on 31 December of each year, starting with data collected for the first full calendar year following [the date of start of application of implementing measures]. These statistics shall be communicated to the Commission on the basis of a standard data communication form annually, by 31 March of the calendar year following the year for which data is collected.

4. The Commission shall establish the communication form referred to in paragraph 3 by way of implementing acts. Those implementing acts shall be adopted in accordance with the advisory procedure referred to in Article 30(2)."

26. Data on business insolvency cases is collected by various agencies for their own distinct purposes. The various sources of data are as follows:

- The Superior Council of Magistracy collects data from courts across the country for measuring the efficiency of the court system. The data collected is predominantly for case management purposes, is not very granular (for instance, it does not provide information on the time taken for the different stages of a procedure, or the recovery rate in case of liquidation), and is not published.

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- The Insolvency Bulletin published by the National Trade Register is a fully computerized system that serves as a tool for notification and summons. It maintains detailed records when an insolvency procedure has been commenced and information captured regarding the duration of procedures is quite comprehensive and granular (e.g. it captures data at virtually every stage in a proceeding and can aggregate it to yield average time taken for each element). However, it has two major limitations. First, although data related to amount and types of claims is embedded in the underlying documents, it is not extracted and therefore the Insolvency Bulletin is not a useful tool for providing information on recovery rates. Second, while the data is public and available free of charge, it must be specifically requested and only very limited data is periodically published and analyzed.[12]

- The National Association of Insolvency Administrators also collects information based on the reports of insolvency practitioners which are largely standardized (e.g. standard form of the table of claims), and this includes information such as rate of recovery and success of the reorganization. However, this information is not published.

27. The authorities intend to enhance their data collection capacity using EU funds. A new component is sought to be added to the Insolvency Bulletin which will enable data related to claims to be captured in a detailed and granular fashion. The module is proposed to be developed with EU funds over the next two years and will be based on the experience in insolvency data collection and analysis in other European countries. Although envisaged predominantly for business insolvency, the module could also usefully be adapted to cover personal insolvency cases.

28. Certain points in the business insolvency procedures could anchor the data collection efforts. The collection of data could take place at various points in the insolvency process (such as petitions, judicial rulings, appeals) which could help gauge the speed of the process (milestones) and identify bottlenecks. Substantive information is generated at a few important points in the process such as through the table of claims, and the reorganization plan (data points). The milestones and the data points could together anchor the data collection framework and provide useful information about the time taken for each element of the process as well as identify the causes of insolvency, the amounts and types of claims, value and types of the debtor's assets, etc. As discussed above, the data collected by the Insolvency Bulletin provides information on milestones, but not data points. Therefore, detailed data is only available regarding the speed of the process. Ideally, data points should supplement the milestones, and the matrix could include the following:[13]

[12] It should be noted that the Insolvency Bulletin routinely publishes limited data on the number of insolvency petitions filed on a monthly basis and offers a comparison with the past year noting the increase or decline in filings. This information, while useful, does not shed light on the effectiveness of the various elements of the insolvency system.

[13] As there are still cases in the courts under the old business insolvency law (Law 85/2006), there could be legacy issues with regard to the data. However, data collected could focus on cases filed after the Code became effective, eliminating this concern.

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Table 3. Possible Milestones and Data Points

Parties	Court	Administrator
Petition (Art. 65 of the Code)	Opening of the Procedure (Art. 71 of the Code)	Appointment of the Interim Insolvency Professional (Art. 73 of the Code)
	Automatic Stay (Art. 75 of the Code) and other interim orders	
	Appointment of Special Administrator (Art. 85 of the Code)	
Submission of Claims		
		Report recommending liquidation or continue with reorganization (Art. 92 of the Code)
		Registration of preliminary table of claims (Art. 92 of the Code)
First creditors meeting (Art. 47-50 of the Code)		Confirmation of Insolvency Professional
Challenge of claims (Art. 111-114 of the Code)	Decisions on challenges	Registration of final table of claims (Art. 112-114 of the Code)
Draft Reorganization Plan (Art. 132 of the Code)		
Vote on Reorganization Plan (Art. 138-139 of the Code)	Confirmation of the reorganization plan (Art. 138-139 of the Code)	
Payments under the reorganization plan	Monitoring	Periodic reports
	Opening of Liquidation	Liquidation of assets and distribution to creditors
		Final report to court (Art. 167 of the Code)
	Closing of Proceeding (Art. 174-184 of the Code)	

E. Recommendations

29. **The recent reforms to the insolvency framework should be implemented in full, and their impact could be enhanced and more effectively monitored.** Changes to the legal framework for business insolvency have brought Romania closer in line with international best practice. The challenges ahead relate to implementing the personal insolvency law and improving

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the business insolvency law further based on the practical experience with its functioning. Additionally, strengthening the systems for data collection and analysis could prove an important monitoring tool for the authorities in their efforts to enhance the impact of the changes. In each of these areas, some specific recommendations are as follows:

Personal Insolvency: With regard to implementing the LII, consideration could be given to:

- Conducting an impact assessment prior to its implementation. The impact assessment should include a review of the adequacy of the existing infrastructure, the costs of implementation, and the impact on the financial sector (which could be pursued in the context of the upcoming Financial Sector Assessment Program).

- Improving inter-ministerial cooperation between the Ministries of Justice, Economy and Public Finance, by establishing a project team with a project manager. The existing action plan should be updated with a strategy for implementation that should be agreed among the Ministries as the appropriate way forward, and based on the strategy, a revised list and sequence of actions along with timelines and the persons responsible and shared across Ministries. Periodic progress reports should be provided to the Ministries and, if practicable, published.

- Providing adequate resources to the CIC to commence work on the secondary legislation, rules and guidance including materials for debtor counseling. The CIC should finalize the standards for insolvency professionals, and qualification examinations could be organized by the professional bodies following which registration of insolvency professionals under the LII could commence.

- Phasing the roll-out of the TICs over a period of 2 years. Establishing 42 TICs, one in each county, could be done in a phased manner with 5-10 TICs being rolled out in the first phase (e.g. by December 31, 2017). After these are successfully functioning, the next phase of 10-15 TICs could be rolled out (e.g. by mid- 2018), drawing from the lessons learned from the first phase of implementation to increase the efficiency of the process. The final phase could establish the remainder of the TICs (e.g. by mid- 2018). Gradual implementation would have the added benefit of reducing the logistics and lowering the budgetary outlay at the outset.

- Monitoring closely the inter-play between the business and personal insolvency laws (e.g. where an individual petitions for both business and personal insolvency, there would be two distinct procedures which could prove onerous and unnecessary, and the discharge under the business insolvency law would be immediate upon liquidation but under the personal insolvency law could take up to five years).

Business Insolvency: With regard to the Code, consideration could be given to:

- Undertaking an evaluation of the functioning of the Code in practice, and consider necessary changes. These could include changes enabling creditors to have an early say in the appointment of the interim judicial administrator including requesting an independent opinion

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on the viability of the debtor; and for small businesses to have access to a simplified and streamlined reorganization procedure.

- Safeguarding against strategic behavior by debtors by ensuring that the insolvency procedures are quick, and adequately supervised through a robust institutional framework including capable insolvency administrators and courts. Where the insolvency process is quick and oversight is robust, strategic debtors can be quickly weeded out. In such cases, the stay would be brief and would not provide debtors with a safe haven for any significant length of time. Delays usually stem from: (i) the design features of the law; and/or (ii) capacity/resource constraints of the institutional framework. Further work could be done to better identify the specific areas where streamlining and strengthening is possible.

- Tax authorities to monitor closely, and as a matter of priority, the cases where (i) the ratio of tax debt to private debt is high, and/or (ii) the amount of the tax debt involved is high. The tax authorities could also monitor the ratio of public debt to private debt in insolvency filings and the recovery rates of private and public creditors. Based on the findings which should be presented to all stakeholders, additional safeguards could be considered if needed.

- Encouraging the use of the pre-insolvency procedures, which are largely out-of-court and could provide a speedy, low cost alternative to the judicial reorganization procedure. The National Bank of Romania and the National Bankers' Association could promote the use of these tools among banks and measures raising awareness among the insolvency practitioners could help.

- Adopting guidance for officials of public creditors that (i) clarifies that public creditors may participate in reorganization plans that do not provide for the payment of public creditor dues in full; and (ii) enables the formulation of a decision on whether or not they could support a debtor's restructuring plan based on the debtor's viability and the private creditors test. Where such guidance is followed in good faith, officials should be protected from personal liability.

- Harmonizing the provisions of the tax and criminal laws with the Code, and provide clear guidance to tax authorities. Consideration could also be given to creating a special group within the tax authority that specializes in insolvency cases and providing them with the requisite training and expertise to handle insolvency cases.

- Strengthening the institutional framework through increasing the number of insolvency judges; providing training opportunities for insolvency judges including inter-disciplinary training and information on international best practice and cross-country experience; and reconsidering the incentive structure for insolvency professionals (in particular fee structure).

Monitoring impact of reforms through data collection and analysis: With regard to data collection and analysis, consideration could be given to:

- Pursuing the enhancements to the Insolvency Bulletin that would enable the data related to claims to be captured for both business and personal insolvency cases.

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- Improving the system of data collection for monitoring the efficiency and effectiveness of the business insolvency framework by designating one agency (possibly, the Romania Insolvency Bulletin) to collect, analyze and periodically publish insolvency case data.

- Standardizing the method of data input at the source producing more granular data that captures the key data points.

- Using periodic reports to identify bottlenecks and propose solutions on an ongoing basis.

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