ANALYSIS OF ARTICLE 138 (6) OF LAW No. 85/2006 ON THE INSOLVENCY PROCEDURE

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Abstract: *Examining the new provisions of article 138 comma (6) which has become article 169 comma (6) of the Government Emergency Ordinance no. 91/ 2013 – Insolvency Code (which is yet not applicable currently) we notice that the legislator opted for the elimination of inadvertencies, errors detected with respect to the analyzed text, yet he did not engage the essence of the problem - the existence of a preliminary procedure of notification resting with the insolvency practitioner and the change of the persons having an active legal capacity in the means of appeal.*

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Until the intervention of Law No. 169/2010, which amended Law No. 85/2006 on insolvency, with respect to the formulation of a second appeal to the sentence of the syndic judge to reject the action in patrimonial liability formulated on the basis of article 138, the common law rules were applicable, i.e. the individual that had the capacity to pursue the proceedings on the merits, has this capacity also as means of appeal. In the case of the examined action, no matter if it was formulated by the insolvency practitioner, by the president of the creditors' committee, by the creditor appointed by the creditors assembly or the majority creditor, every one of them acquired the capacity to pursue the active proceedings on the merits and, therefore, could formulate the appeal.

Currently, article 138 comma (6) of the Law indicates that in case a sentence of rejection of the action launched on grounds of comma (1) (by the insolvency practitioner) or, as the case may be, comma (3) (by the president of the creditors committee, the creditor appointed by the creditors assembly, the majority creditor), the official receiver/ the liquidator in bankruptcy who does not intend to formulate an appeal against it shall notify the creditors with respect to his intention. If the general assembly or the creditor that owns more than half of the value of all the debts decide that an appeal must be formulated, the official receiver must formulate the means of appeal in accordance with the law.

We will prioritize the clarification of inadvertencies found in the legal text and then analyze the provisions of the legislator.

The first issue that we submit to analysis refers to the elimination of the liquidator within the framework of formulation of the appeal to the sentence rejecting the action in patrimonial liability of the members of the debtor management and/ or supervision bodies.

Although the first thesis of comma (6) discusses the notification obligation of the official receiver or of the liquidator, the second thesis of the same comma imposes the obligation to formulate the appeal only to the official receiver. This situation may lead to two hypotheses.

In a first case we accept that the intention of the legislator, as it expressly results from the legal provision being analyzed, was that the appeal be promoted only by the official receiver.

This leads to the conclusion that the action in liability be judged on the merits and as means of appeal only within the framework of the general procedure - during the observation period and the reorganization period - . We are saying this because within the framework of the simplified procedure and during the liquidation period in the general procedure we meet the liquidator and not the official receiver. We reject this hypothesis because article 140 shows the destination of the amounts obtained following the execution of the payment obligation established in the sentence of commitment of liability, respectively in reorganization for the payment of debts according to the payment schedule or completion of the necessary funds in order to continue the activity of the debtor, and, in case of bankruptcy, to cover the liabilities. This imposes the rule that the demand to commit the liability may be formulated both in the reorganization procedure and in the bankruptcy procedure. By not accepting the situation that only in the general procedure - during the observation period and the reorganization period - there may be formulated the action in liability, in the absence of a legal provision we may suppose that in the liquidation, the legislator allows creditors (the president of the creditors committee, the creditor appointed by the creditors assembly or the majority creditor) to formulate the appeal. This situation would suppose the establishment of the active capacity to pursue the proceedings based on the stage of the insolvency process. If we are in a general procedure, during the observation or the reorganization procedure, the appeal will be promoted by the official receiver, while in liquidation in a general procedure and in the simplified one, the creditor who initiated the merits of the case will also be able to promote the appeal. Under these circumstances, if a general procedure was opened it is possible for the official receiver to formulate the demand of commitment of liability, while by moving on to the simplified or the liquidation procedure, the appeal might be promoted by one of the creditors authorized by the law. However, we think that such an exception hypothesized an express regulation of the legislator.

In the second situation we accept that the intention of the legislator was that the appeal be promoted by the official receiver or by the liquidator and that this non-correlation of the text is a simple error or a legislative omission. We opt for the adoption of this hypothesis because the action in liability may be formulated, mainly, in accordance with article 138 comma 1 by the insolvency practitioner, no matter if he/she is appointed official receiver or liquidator.

A second issue that can be noticed in comma (6) of article 138 of the Insolvency Law refers to those who have the right to compel the insolvency practitioner to formulate the appeal. In the text we find that the ”general assembly” and the majority creditor have this right. Whereas the majority creditor is the one who owns more than half the value of all debts, the ”general assembly” is not defined. Reading Law No. 85/2006 we can find a similar expression in article 18 where, as far as the special administrator is concerned, it is specified that „after the opening of the procedure, the general assembly of the shareholders / partners of the debtor, a legal person, he shall appoint , at their expense, a representative...”. The shareholders / partners of the debtor, respectively the general assembly of the shareholders / partners do not even have the capacity to participate in the procedure, inasmuch as their interests are represented under the conditions of article 18 by the special administrator and under the conditions of article 3 point 26 by a special conservator. For these reasons we believe that we must exclude the alternative in which the general assembly of the shareholders/partners acquires a unique right within the framework of the insolvency procedure to decide on the promotion of the appeal against the sentence of the syndic judge to reject the action to commit the liability of the members of debtor management and/or supervision bodies.

An version that we consider plausible is the one in which the legislator took into consideration the creditors assembly for the exercise of the right to compel the insolvency practitioner to promote the appeal. We opt for this interpretation of the legal

text because it is the president of the creditors committee, the creditor appointed by the creditors assembly if a committee was not constituted and the majority creditor who have the active subsidiary capacity to pursue the proceedings (following the insolvency practitioner) when formulating the action in liability. The acquisition of this capacity by the president of the creditors committee and the creditor appointed in the absence of a creditors committee is conditioned by the vote expressed in the creditors assembly. The majority creditor, instead, is not conditioned by this vote. He represents more than half the liabilities of the debtor. Following the juridical logic of the legislator as much as the formulation of the demand to commit the liability by creditors, it seems natural that the right to compel the insolvency practitioner to promote the appeal should belong with the creditors assembly or the majority creditor.

In the light of what we have said so far, we consider that in comma (6) of article 138 of Law 85/2006 there is a typing error in the legal text, i.e. the expression used there, ”general assembly” must be understood as ”creditors assembly”

With respect to the analysis of the legal provisions, comma (6) of article 138 regulates the conditions under which the insolvency practitioner is going to promote the appeal against the action to commit liability of the management and/or supervision body members. We notice that in the appeal stage it doesn't seem to be relevant anymore who formulated the merits of the action, i.e. that only the insolvency practitioner has the capacity to formulate the appeal.

We reject the opinion expressed in the doctrine that the applicability of comma (6) only exists in case the demand to commit the liability was formulated exclusively by the official receiver/liquidator, because the legal text expressly refers to the situation in which the action was formulated by the creditors who may acquire the capacity to pursue the proceedings in accordance with article 138 comma 3 of Law No. 85/2006. (Munteanu, 2011, p.9)

The Law provides for the obligation to notify the creditors, to be performed by the insolvency practitioner, with respect to his intention not to promote an appeal against the rejection of the sentence of commitment of the patrimonial liability of the members of management bodies. Thus, no matter if the initial action is formulated by the insolvency practitioner or by the creditors who acquire this procedural right, the former is compelled to notify the creditors with respect to his lack of interest to promote the appeal.

On the one side, if the insolvency practitioner formulates the demand to commit liability, being convinced that the members of the debtor management and/or supervision bodies, by means of their illicit deeds have brought the company to insolvency, it seems natural to use the means of appeal in order to support the reasoning before the superior courts of law. We must not forget that he does not act in his own name, but in the collective interest of the creditors and to maximize the assets of the debtor is one of his attributions.

On the other side, if the insolvency practitioner was not able to identify the individuals to be held responsible for the insolvency state or based on an analysis of the accounting documents he decided that it is not appropriate to introduce this action, the creditors will see their way open to exercise this right. Therefore we cannot identify the reasoning of the legislator when compelling the insolvency practitioner to notify his intention not to file an appeal against an action with respect to which he has already decided that it does not contain the necessary elements so as to discuss it on the merits of the case.

The notification of the insolvency practitioner related to his intention not to promote the appeal, in the absence of a contrary provision, will be published in the Insolvency Proceedings Bulletin. Article7 of Law No. 85/2006 defines as a general rule that the summoning of the parties as well as the communication of all proceeding

documents, of the convocations and notifications are to be published in the Insolvency Proceedings Bulletin and among the exceptions we cannot find the notification of the insolvency practitioner toward the creditors, related to his intention not to promote the appeal.

As a consequence of this notification if the creditors assembly or the majority creditor decide that it is necessary to file an appeal, the insolvency practitioner must formulate the means of appeal. This provision is an innovation in the Insolvency Law and a waiver of the common right, which, as a principle, establishes that the parties in the file of first instance have the capacity to promote the means of appeal as well.

The hypothesis in which the decision must be made by the majority creditor does not raise issues because it refers to the sentence of a single creditor without going through a preliminary proceeding. Yet, the hypothesis in which the decision to promote the appeal belongs with the general assembly this entails the realization of several stages. In the first place the creditors assembly will have to be summoned either by the official receiver/liquidator or by the creditors committee, or upon request of the creditors who own liabilities of at least 30% of their total value. (Article 13 of Insolvency Act No. 85/2006)

Regardless of the initiator of the convocation it has to be published in the Insolvency Proceedings Bulletin. The decision of the creditors assembly, included in a minute shall be lodged, care of the insolvency practitioner, in the case file, within two working days from the date on which the creditors were summoned to express their opinion with respect to the promotion of the appeal. (Article 14 (6) of Insolvency Act No. 85/2006)

Inherently, we raise the question of the role of this intermediate proceeding, prior to the appeal. We believe that this prior procedure only represents the modality established by the legislator to compel the insolvency practitioner to promote the appeal and not a condition to acquire the active capacity to pursue proceedings. Therefore, every single time the appeal court notices the formulation of the means of appeal by the insolvency practitioner, it will not perform a verification of the way in which the active capacity to pursue the proceedings was acquired.

In our opinion, going through this stage, expressing the decision of the majority creditor or of the creditors assembly, is meaningless. Inherently, the creditors will opt for the promotion of the appeal against the sentence to reject the action in liability provided by article 138. Finally, the purpose of this action is the very payment of the liabilities to the creditor. It would be a lack of juridical logic to think that the creditors are willing to give up a possibility to receive the liabilities which haven't been paid by the debtor. Moreover, both the creditors assembly and the majority creditor expressed their intention to recover part of the liabilities from the members of the management bodies when they promoted the action pursuant to article 138, a context in which we believe that a double agreement related to the same action is necessary, i.e. expressed initially for the filing of the action and successively for the promotion of the appeal.

It must be said that following the reading of article 138 comma (6) it does not emerge with certainty that it is only the insolvency practitioner who is going to acquire an active capacity to pursue proceedings in the formulation of the appeal to the sentence of rejection of the action in patrimonial civil liability of the members of the management bodies. The law text related to the obligation of the insolvency practitioner to formulate the appeal finds its application in both cases instituted by the legislator for the formulation of the action in patrimonial civil liability (article 138 comma 1 and comma 3), i.e. it can be deduced that it is only official receiver/liquidator who is entitled to formulate the appeal. However, the active capacity to pursue the proceedings in the formulation of the action in liability also lies with the president of the creditors committee, the creditor appointed by the creditors assembly and the majority creditor,

while the legislator does not decree anything with respect to the elimination of such capacity in the matter of appeal.

Indeed the law does expressly state that the insolvency practitioner may be compelled under certain circumstances to promote the appeal, but in our opinion this fact does not automatically eliminate the possibility for the creditors who have formulated the action in patrimonial liability to promote the appeal as well. In our opinion comma (6) of article 138 does not contain any interdiction related to the filing of the appeal by the creditors entitled by the law to formulate the merits of the action; moreover, we believe that in this case the creditors have a right of option. Their option refers on the one side to the possibility to compel the insolvency practitioner to promote the appeal and on the other side to the possibility of the creditor who has formulated the action in patrimonial liability to formulate the means of appeal. In this hypothesis, although the law seems permissive with respect to the formulation of the appeal by the creditors who have promoted the action on the merits as well, we cannot understand the reason for which such an elaborate proceeding to compel the insolvency practitioner to formulate the appeal should be instituted.

If it is accepted that the appeal is also accessible for the creditors who had the right to formulate the action on the merits, we notice that there is a reason which could determine the creditors assembly or the majority creditor to compel the insolvency practitioner to formulate the means of appeal, i.e. the legal expenses. In accordance with the article 77 of Law No. 85/2006 all the actions introduced by the official receiver or by the liquidator in application of the provisions of the insolvency Law, including those meant to recover the liabilities, are exempt from the legal stamp duty. Thus, if the appeal is introduced by the insolvency practitioner, the creditors will no longer pay the duties related to the promotion of the means of appeal. For the creditors, the promotion of the appeal entails the payment of certain stamp duties according to Law No. 146/1997. These duties are to be paid in advance, at the latest until the first trial date and the failure to observe this requirement is sanctioned by the annulment of the demand for appeal. (Court of Appeal of Timisoara, Decision No. 744 of June 8, 2010 in File No. 3/115/2009)

In practice, this system is used to reach the desired objective - the promotion of the appeal - , but by means of another procedure, different than the one provided for by the law. Therefore, on the occasion of the first assembly of the creditors, they mandate the insolvency practitioner to formulate the appeal under the conditions in which the demand to be formulated will be rejected by the syndic judge. (Law Court of Timisoara, file No. 9711/30/2008; Law Court of Caras Severin, File No. 5826/115/2010, File No. 1442.0/115/2010, File No. 1534/115/2010)

In the light of what has been already mentioned we believe that instituting a complex preliminary proceeding in order to promote the appeal against the sentence to reject the action in patrimonial liability must find itself a more clear purpose, different than the payment of the stamp duties.

The enouncement of the reasons for the introduction of comma (6) of article 138 is not probatory either to this end. The author of the legal initiative indicates that "the continuation of the appeal proceeding as a consequence of the rejection of the demand to commit the material liability of the manager, in his own name, is also a material risk for the insolvency practitioner, inasmuch as the approval and involvement of the creditors and especially of the majority creditor are equally necessary. Judging by the enouncement of the reasons, it seems that what was actually intended was the possibility to compel the insolvency practitioner to promote the appeal when the action that he formulated is rejected by the syndic judge. In fact, it was only the continuation of the legal steps when the action of the insolvency practitioner was rejected that was addressed. yet, this explanation is in contradiction with the regulation instituted by the

legislator which provides for the compulsoriness of formulation of the appeal by the insolvency practitioner, regardless of whether the action was formulated by him or by the creditors to which the Law No. 85/2006 grants this capacity. (Originator Representative Mircea Grosaru, The Parliamentary Group of National Minorities)

In consideration of a legal text that can have multiple interpretations and in the absence of a doctrinal opinion in this merit we believe that the creditors have a right of choice between formulating the means of appeal and compelling the insolvency practitioner to promote the appeal. In our opinion, the legislator establishes that the appeal against the rejection of the sentence to commit the liability pronounced by the syndic judge may be promoted by any one of the holders of the capacity to pursue the proceedings, with the optional possibility to compel the insolvency practitioner to formulate it.

We believe that instead of the clear and simple system established by the common la in the matter of appeal, in the insolvency law, as far as the commitment of liability is concerned, an ambiguous and complicated system was instituted. In fact, after the rejection of the sentence of commitment of liability by the syndic judge, a series of stages must also be gone through until the formulation of the appeal. These stages address: a notification published by the insolvency practitioner in the Insolvency Proceedings Bulletin with respect to his intention not to promote an appeal; a summoning of the creditors assembly that will be published in the Insolvency Proceedings Bulletin (when no majority creditor is present in the case), the pronunciation of a sentence of the majority creditor of the creditors assembly meant to compel the insolvency practitioner to promote the appeal. In this context we must say that the term for appeal is of seven days from the communication of the sentence of the syndic judge.

It is easy to notice that going through these stages hypothesizes a time period of more than 7 days, which means that the term within which the appeal could be filed would expire. A solution in order to file the appeal on time would be that, after the rejection of the action in liability, the insolvency practitioner should lodge his intention to formulate the means of appeal, while the reasons could be indicated until the first trial date at the Court of Appeal. We pointed this out on condition that after having gone through the legal stages, the goal be the same, i.e. the insolvency practitioner will be compelled to promote the appeal.

The waiver of the common law should find its reasoning in the collective nature of the proceeding. In case the insolvency practitioner has formulated the action in liability, rejected by the syndic judge, we understand that the creditors assembly or the majority creditor may decide that the practitioner can continue the trial with the appeal. This aspect corresponds to the reasons expressed by the initiator of the legal amendment. We are reiterating the idea that the official receiver / liquidator has legal obligations to maximize the assets of the debtor even by using the mechanism instituted by the article 138, and to the extent to which he thinks he owns all the elements to formulate such an action, he will maintain, inherently, his conclusions in the means of appeal as well, while a decision of the creditors to this end is not necessary.

If the insolvency practitioner decides he will not formulate the action in patrimonial liability, it is formulated by the creditors and rejected by the syndic judge, the issue raised is the right of the general assembly or of the majority creditor to compel the insolvency practitioner to formulate the appeal. The decision of the official receiver/ liquidator not to promote the demand for commitment of liability is registered and justified in the report drawn up according to article 59 regarding the causes and the circumstances of the insolvency state, indicating the individuals which can be hold responsible for such state. This decision may be made taking into consideration two aspects: on the one side the impossibility to indicate the people to be held responsible

because of the lack of relevant documents related to the activity of the company and, on the other side, a relevant analysis of the accounting documents that should indicate either that the acts of the members of the management and/or supervision bodies are not the ones provided for by article 138 comma 1 lett. a-g, or, whether expressly indicated acts have been identified, these acts did not directly lead to the insolvency state of the debtor. This analysis must be found in any insolvency case file and failure to perform it might be sanctioned by the creditors by replacing the insolvency practitioner.

Consequently, following a motivated decision of the insolvency practitioner not to formulate the demand for commitment of liability, the law compels him to formulate the appeal against the sentence to reject the action filed by the creditors. We believe that the practitioner is put by the legislator in a difficult situation, i.e. to act against his own convictions, against his own conclusions that bear the mark of the professionalism of every insolvency practitioner. Inherently we can question the quality of the judicial process performed against one's own will.

The attributions of the official receiver/liquidator in the insolvency proceeding are guided towards realizing the goal set by the insolvency law, i.e. the payment of the liabilities to the creditors, which also involves the representation in court of their collective interest. We think that compelling the insolvency practitioner to formulate an appeal against an action with respect to which he expressed the decision that it is not necessary to promote cannot be the object of the representation of the collective interest of the creditors. The management of the insolvency proceeding hypothesizes the control of the decisions of the insolvency practitioner, as far as opportunity is concerned, by the creditors. This right to control cannot be interpreted as a possibility of the creditors to compel the official receiver / liquidator to act against his own specialty decisions.

The activity of the insolvency practitioner is a regulated one, i.e. he is appointed to the offices of official receiver or liquidator precisely because of his certification as an expert in this matter. The code related to the ethical behavior issued by the National Association of insolvency practitioners indicates in article 3 the fundamental principles that must be observed with respect to the activity of the insolvency practitioner: independence, moral integrity, observance of the professional secret, etc. We believe that the insolvency practitioner is deprived of a fundamental principle which should govern his activity, namely the principle of independence, since he is compelled to support a means of appeal which goes against the expert opinion that he lodged in the case file.(GEO No. 86/2006)

Although currently these are the applicable rules, in the matter of formulation of the appeal against the sentence of the syndic judge to reject the action in patrimonial liability formulated according to article 138 of Law No. 85/2006, we must not leave out the fact that Romania is undergoing a process of profound legislative reform. The Civil Code entered into force on October 1, 2011, the Civil Procedure Code entered into force on February 15, 2013, and the Penal Code and the Penal Procedure Code on February 1, 2014. There must be said that the coming into force of the Civil Code led to the rescission of a large part of the Romanian Commercial Code. This complex process affected the insolvency domain as well. On November 1, 2011, the Ministry of Justice announced that it initiated the works for drafting the Insolvency Code, approach for which it received technical assistance from a consortium made up of specialized insolvency firms. On October 4, 2013, the Government Emergency Ordinance no. 91/ 2013 – Insolvency Code was published in the Official Bulletin of Romania. The Insolvency Code entered in force on October 25, 2013 and, surprisingly, its application was suspended on November 1, 2013, the Insolvency Code being declared unconstitutional, a context in which the Law No. 85/2006 on the insolvency procedure is still applicable.(Decision 447/29 October 2013, Constitutional Court of Romania)

Examining the new provisions of article 138 comma (6) which has become article 169 comma (6) of the Government Emergency Ordinance no. 91/ 2013 – Insolvency Code (which is yet not applicable currently) we notice that the legislator opted for the elimination of inadvertencies, errors detected with respect to the analyzed text, yet he did not engage the essence of the problem - the existence of a preliminary procedure of notification resting with the insolvency practitioner and the change of the persons having an active legal capacity in the means of appeal.

We believe the introduction by the legislator in comma (6) of article 138 of Law No. 85/2006 of a new own system to formulate the means of appeal against the action in patrimonial liability in insolvency is inapposite. The ambiguous and interpretable provisions of the legal text, colligated with the institution of a real procedure to formulate a means of appeal make us believe that the regime of the common law in this matter is preferable. In our opinion, the rules which can be applied to the common law in the matter of the means of appeal should have been specified, that is the person who held the capacity to formulate the action in liability before the first instance will also have the capacity to formulate the means of appeal.

Right now, the Government sent to the Parliament the Insolvency Code as a law draft, which should give the legislator an opportunity to also consider either the profound reform of the analyzed article or its elimination.

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