INSOLVENCY AND BANKRUPTCY OF COMMERCIAL COMPANIES

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RESEARCH ARTICLE

Abstract

According to Article 5 of Law no. 85/2014:"Insolvency is the state of the debtor who is unable to pay their due debts, in other words, the situation in which the debtor can no longer fulfill their payment obligations to creditors within the established timeframe."According to Article 132 of Law no. 85/2014:"Bankruptcy is the state of the debtor undergoing insolvency proceedings who can no longer be reorganized, and whose activity is liquidated in order to cover as much of their debts to creditors as possible." These regulations apply within the specific insolvency procedures provided by law and are essential for protecting both debtors and creditors in the process of managing financial difficulties.

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INTRODUCTION

In an era of economic globalization, where markets are increasingly interconnected and vulnerable to economic and financial fluctuations, the concepts of insolvency and bankruptcy have acquired particular significance within commercial law. These two legal processes are essential for maintaining economic balance, enabling both the protection of debtors facing financial difficulties and the safeguarding of creditors' rights. In this context, legislation on insolvency and bankruptcy plays a fundamental role, aiming to restore the financial balance of economic entities while also regulating the management of their assets to ensure maximum debt recovery.

Insolvency represents a legal and financial situation in which a commercial company is unable to meet its payment obligations to creditors when due. It does not automatically signify the closure of the business but rather the initiation of a legal process designed to identify solutions for debt restructuring and the continuation of operations. Law no. 85/2014 on insolvency prevention and insolvency proceedings was introduced in Romania to provide a modern legislative framework adapted to the requirements of the European Union, aiming to support companies in financial difficulty by allowing them to access business reorganization and debt restructuring procedures. The insolvency procedure is based on the principle of business continuity, offering companies in difficulty the opportunity to maintain operations and reorganize in a sustainable manner. [3]

Although insolvency may be seen as an opportunity for restructuring, the process is not always sufficient to save the company. In certain situations, insolvency may inevitably lead to bankruptcy, especially when reorganization is not possible or when the company's assets are insufficient to cover its debts. Bankruptcy is, therefore, the final stage of the insolvency process, characterized by the liquidation of the company's assets and their distribution among creditors in the legal order of priority. The purpose of bankruptcy proceedings is to maximize the value of the company's assets and recover as much as possible for creditors. Despite the legal provisions, bankruptcy can have a significant negative impact on the economy, employment, and the economic reputation of the state. [4]

In Romania, insolvency and bankruptcy procedures have been significantly regulated through Law no. 85/2014, which replaced the previous regulation from 2006. This legislative framework is oriented both toward protecting creditors and rehabilitating debtors through judicial reorganization. The law establishes a series of legal mechanisms that allow for better management of companies' financial difficulties and ensures a transparent and fair procedure for all participants in the process. However, despite the progress brought by the new legislation, its implementation is often marked by challenges such as disputes between creditors and debtors, negative perceptions of the insolvency procedure, and difficulties in implementing reorganization plans. [5]

In this context, this paper aims to analyze in detail both the theoretical and practical aspects of insolvency and bankruptcy in commercial companies in Romania. We will explore the current legal regulations, analyze the insolvency process, the differences between insolvency and bankruptcy, and their impact on the economy. Furthermore, emphasis will be placed on the analysis of practical cases and the assessment of the effectiveness of bankruptcy prevention and debtor reorganization mechanisms, as well as on the difficulties encountered by entrepreneurs and competent authorities in applying the legislation.

Thus, this study aims to deepen the understanding of insolvency and bankruptcy processes, highlight existing regulations, and propose solutions to improve them in the context of the Romanian economy.

MATERIAL AND METHOD

The materials used to write this work consist of normative acts, books, articles and websites. The methods used are legal, namely the formal method, the comparative method, the logical method and the analytical method. The use of these methods had the role of carrying out a systematic analysis of the information from the studied sources in order to elaborate the points of view, the results of the research carried out and the conclusions.

RESULTS AND DISCUSSIONS

Insolvency is the legal condition in which an entity, whether an individual or a legal person, is no longer able to pay its debts when due. It can be initiated by the debtor or by creditors and may lead to the opening of a legal procedure aimed at helping manage debts and, in some cases, restructure the business to avoid bankruptcy.

1. Characteristics of Insolvency

- Inability to pay – The debtor can no longer pay debts at maturity, which is one of the fundamental traits of insolvency. This does not mean the debtor lacks assets or income, but rather that they do not have enough liquid resources to meet due obligations.
- Inability to meet creditor demands – The debtor is unable to meet creditors' demands or pay all debts, which may lead to a request to open insolvency proceedings. The process begins at the request of either the debtor or one of the creditors.
- Protection of creditors and the debtor – During the insolvency procedure, the debtor benefits from protection against individual actions by creditors, who are required to participate in a coordinated process to recover debts. The goal is to maximize recovery value for all creditors, while respecting the legal priority of claims.
- Possibility of reorganization – Insolvency does not automatically imply bankruptcy. It allows the debtor to submit a judicial reorganization plan, which may include debt restructuring and operational adjustments to attempt financial recovery.

2. Steps in the Insolvency Procedure

- Opening the insolvency procedure – Insolvency is triggered by a petition filed with the competent court. The petition may be submitted by the debtor (acknowledging financial difficulties) or by one or more of their creditors. The court will analyze the petition and, if it finds that the debtor is in a state of insolvency, will initiate the procedure.
- Appointment of a judicial administrator – After opening the procedure, the court appoints a judicial administrator or insolvency practitioner. This person will manage the debtor's affairs throughout the process, analyze the debtor's financial situation, and, where possible, propose a reorganization plan.
- Establishment of a reorganization plan – If the debtor wishes to continue operations, the judicial administrator can propose a reorganization plan. This may include measures such as debt restructuring, extension of payment terms, or asset sales to cover debts. The plan must be approved by a majority of creditors and by the court.
- Verification and admission of claims – Creditors must submit their claims, which are reviewed for validity by the judicial administrator. A creditors' list is then drawn up, detailing the priority ranking and payment structure of claims.
- Reorganization or liquidation procedure – If the reorganization plan is approved and successfully implemented, the company can continue its operations and exit insolvency. If reorganization is not possible, the court may open liquidation proceedings, during which company assets are sold to pay off creditors.

- Closure of the insolvency procedure – The procedure ends when the debts are paid or if there are no remaining assets to cover them. In the case of successful reorganization, the company exits insolvency and resumes normal operation. If liquidation is required, the assets are sold and debts are paid in accordance with the creditors' priority order.

3. Types of Insolvency

a. General Insolvency Procedure

- Definition: The general insolvency procedure is regulated by Law no. 85/2014 and applies when a company or legal entity is no longer able to meet its financial obligations, entering a state of payment incapacity. This includes the potential for both reorganization and liquidation.
- Who it applies to: Primarily applicable to legal entities (commercial companies, economic operators) that are unable to pay their debts at maturity.
- Why it applies: It aims to protect the interests of both debtors—who may try to restructure their business—and creditors—who seek to recover at least part of their debts. The procedure may lead to economic reorganization to avoid bankruptcy.
- When it applies: It is opened when the debtor is found to be insolvent—unable to pay debts on time and lacking sufficient assets to meet obligations. This can be established by the debtor or a creditor.
- Differences from other procedures: This is the standard procedure for most legal entities in financial distress. Compared to other procedures (e.g., simplified insolvency for individuals), this involves more complex legal mechanisms and allows for reorganization or liquidation.

b. Simplified Procedure for Individual Debtors

- Definition: The simplified insolvency procedure for individual debtors is designed exclusively for natural persons who are unable to pay their debts. It is a less complex and faster process than the general one.
- Who it applies to: Only to individuals (not legal entities) in a state of insolvency who cannot pay accumulated debts. Typically, these are individuals with lower debts and fewer assets compared to businesses.
- Why it applies: The goal is to offer a quick and accessible solution for individuals overwhelmed by debt, protecting them from abusive creditors and giving them a chance to reorganize their financial life more simply and cost-effectively.
- When it applies: It is initiated when an individual cannot pay debts on time and lacks the resources or assets to cover them. This applies in cases of financial hardship with minimal assets to liquidate.
- Differences from other procedures: Unlike the general procedure, this is much simpler and aimed at individuals without the complexity of commercial entities. The reorganization process is more flexible and usually does not involve detailed restructuring plans.

Judicial Reorganization Procedure

- **Definition**: The judicial reorganization procedure applies to legal entities (commercial companies) facing financial difficulties but that can be salvaged through the restructuring of debts and economic activity. Its purpose is to offer the debtor a chance to recover their business.
- **Who it applies to**: This procedure applies to commercial companies (legal entities) that, although insolvent, have the potential to reorganize and become economically viable, thereby avoiding bankruptcy.
- **Why it applies**: It aims to protect the business, its employees, and creditors by offering an alternative to asset liquidation. If the business is properly restructured, it can return to profitability and ensure debt repayment over a longer period, reducing losses for all parties involved.
- **When it applies**: The judicial reorganization procedure is used when the court deems the debtor's activity to be salvageable and there is a viable restructuring plan that can address the insolvency and offer solutions to creditors.
- **Differences from other procedures**: Unlike the general procedure, which may lead directly to liquidation, judicial reorganization allows the company to continue its economic activity and focuses on recovery. It involves drafting a detailed reorganization plan, unlike the simplified procedure for individuals.

Asset Liquidation Procedure

- **Definition**: The asset liquidation procedure refers to the process by which the assets of a company or an insolvent individual are sold to pay creditors. This is the final step when reorganization is no longer an option.
- **Who it applies to**: It applies to both legal and natural persons when reorganization is not possible and there is no chance to save the business. The procedure is intended for those

unable to pay debts or continue economic activity.

- **Why it applies**: It applies when reorganization fails or is not feasible, and the primary goal becomes paying off debts as much as possible. Liquidation is the last resort and the final stage of the insolvency process, where assets are sold and the proceeds are distributed among creditors.
- **When it applies**: It is used when the judicial reorganization procedure has failed or when no viable path exists to restore the debtor's activity, making business continuation impossible.
- **Differences from other procedures**: Liquidation is the final procedure that ends the debtor's business activity, unlike reorganization which aims for recovery. Unlike the simplified procedure for individuals, liquidation may involve a more complex asset sale and creditor distribution process.

The Role of the Court and Judicial Administrator in the Insolvency Procedure

In the insolvency procedure, the court and judicial administrator have essential roles in ensuring the proper conduct of the process:

a. The Court

The court is responsible for examining the application to open insolvency proceedings and appointing the judicial administrator. It also approves or rejects reorganization plans proposed by the debtor or administrator. If liquidation is necessary, the court supervises the sale of assets and distribution of funds among creditors.

b. The Judicial Administrator

The judicial administrator plays an active role in managing the insolvency procedure. They take control of the debtor's activity, analyze the financial condition, and propose solutions to save the business (via reorganization) or, in case of bankruptcy, supervise asset liquidation. The administrator must act in the interest of creditors and comply with the law throughout all stages of the process.

Bankruptcy

1. Characteristics of Bankruptcy

- **Judicial nature of the procedure**: Bankruptcy is a court-regulated procedure, governed by law and supervised by judicial authorities. It starts with a petition filed with the competent court, which decides whether to open the procedure based on presented evidence. The court ensures legal compliance and protects the rights of creditors and the debtor.
- **Universality of the procedure**: Bankruptcy is universal, meaning all of the debtor's assets are included in the process and all debts are handled under one case. All creditors may participate, and the money obtained from asset liquidation is distributed in accordance with legal priority.
- **Public nature of the procedure**: All bankruptcy procedure stages are public, and information is accessible to all participants—creditors, the debtor, and authorities. Transparency ensures protection of everyone's rights.
- **Special protective measures for the debtor**: During the bankruptcy process, the debtor benefits from temporary protection against enforcement actions by creditors. This means that, during the procedure, creditors cannot initiate individual recovery actions. The purpose of this protection is to offer the debtor a chance to reorganize the business or reach a settlement with creditors.
- **Collective nature of the procedure**: Bankruptcy involves all creditors collectively. They are grouped into a single case, and the court's and administrator's decisions apply to all, following the legal order of payment priorities.
- **Closure of the procedure**: Depending on the outcomes—full asset liquidation or successful reorganization—the bankruptcy case may end with its closure. If all debts are paid or if there are insufficient funds, the court may decide to close the case.

Steps in the Bankruptcy Procedure

- **Opening the bankruptcy procedure**: Bankruptcy proceedings begin through the initiation of insolvency proceedings, requested by either the debtor or the creditors. The petition is filed with the competent court, which evaluates the debtor's insolvency status. If the court finds the debtor unable to meet due obligations, it issues a decision to open the insolvency procedure, which is then published.
- **Appointment of a judicial administrator**: Once proceedings are opened, the court appoints a judicial administrator or insolvency practitioner responsible for overseeing the debtor's activities and managing the insolvency case. The administrator protects creditor interests and ensures a fair process, including evaluating and inventorying the debtor's assets.

- **Drafting and implementing a reorganization plan**: The debtor or administrator may propose a reorganization plan, including measures such as debt restructuring, reductions, or operational changes. This plan must be approved by a majority of creditors. If it is rejected, the liquidation of the debtor's assets follows.
- **Asset liquidation**: If reorganization is not feasible or approved, the debtor's assets are liquidated. Liquidation involves selling the debtor's assets to pay off debts. This is done via public auctions or other methods permitted by law. [7]
- **Closure of the bankruptcy procedure**: The procedure ends after asset liquidation and distribution of funds to creditors in the legal priority order. If all debts are settled or if available funds are insufficient, the court orders the closure of the case.
- **Effects of bankruptcy on the debtor**: Bankruptcy has major implications for the debtor, including loss of control over the business and potential dissolution of the legal entity. The debtor may also face restrictions in starting new businesses or obtaining credit. [7]

CONCLUSIONS

Insolvency and bankruptcy are two essential concepts in commercial law and financial business legislation. Although they are often used interchangeably, they represent different stages of a legal process, each with distinct purposes, implications, and procedures. In this conclusion, we will analyze the fundamental differences between insolvency and bankruptcy, focusing on definitions, procedures, effects, and the impact on both debtors and creditors.

Insolvency is an economic condition affecting a natural or legal person who can no longer meet their due debts but may undergo a reorganization process to recover. Insolvency is therefore a broader concept, referring to the temporary inability to meet financial obligations, which can potentially be overcome through business restructuring.

By contrast, bankruptcy is a specific legal procedure that occurs when insolvency cannot be resolved through reorganization.

Bankruptcy represents the final stage of the insolvency process, when there is no prospect for the debtor's recovery, and the debtor's assets are liquidated to satisfy creditors' claims, as far as possible. Bankruptcy involves a formal procedure of asset liquidation and may lead to the dissolution of the debtor entity in the case of a legal person, or to a declaration of personal incapacity to repay debts in the case of a natural person. [8]

In the insolvency procedure, the debtor has several options for financial recovery. The law allows for the drafting of a reorganization plan that may include measures such as rescheduling payments or reducing debt amounts. A court-appointed judicial administrator oversees the implementation of this plan, and the debtor continues operations under the condition that deadlines are met. If the reorganization is successful, the debtor may exit insolvency and continue activity without entering bankruptcy. [10]

On the other hand, the bankruptcy procedure comes into effect when reorganization is no longer possible or has failed. Bankruptcy involves the liquidation of the debtor's assets to obtain funds that will be distributed among creditors according to a plan established by the court and the judicial administrator. In bankruptcy, if the assets are insufficient to cover the debts, the procedure ends without full repayment to creditors. Bankruptcy may lead to the dissolution of the company or to the loss of financial capacity in the case of individuals, who are no longer permitted to manage property or businesses.

Insolvency provides the debtor with temporary protection, as they benefit from a moratorium that prevents creditors from initiating enforcement actions during the procedure. This represents an opportunity for the debtor to restructure their business, renegotiate debts, and relaunch economic activity. Creditors also actively participate in the reorganization process, being consulted and involved in decisions related to the debtor's restructuring. [10]

However, in bankruptcy, the debtor's protection gradually fades, and control of the activity is entirely transferred to the judicial administrator. Bankruptcy seriously affects the debtor's reputation, especially for legal entities, as it can lead to dissolution and loss of the right to conduct economic activity for a limited or even permanent period. Creditors, on the other hand, are unlikely to recover their full claims and must participate in the liquidation process in hopes of recovering as much as possible from the remaining assets.

In many cases, insolvency is an effective solution for overcoming a temporary financial crisis, serving to prevent the bankruptcy of a potentially viable long-term business. Furthermore, the insolvency process may preserve jobs and business relationships, providing long-term economic benefits. Reorganization can include development or restructuring strategies that help businesses adapt to new economic conditions. [9]

Conversely, bankruptcy has a significantly negative economic impact. The liquidation of assets affects not only the debtor but also all creditors, employees, and other stakeholders. Bankruptcy can lead to substantial financial losses for creditors, and in the case of a legal entity, it can impact the entire local or national economy, especially if the company is large or plays a key role in essential economic sectors. [9]

The main difference between the two lies in the potential for recovery: in insolvency, the entity may restructure its debts and avoid closure, while bankruptcy involves the definitive liquidation of the business. Thus, insolvency procedures can offer a path out of financial crisis, whereas bankruptcy typically signifies the end of an economic chapter.

Insolvency and bankruptcy are essential legal concepts for understanding how an entity can enter a serious financial condition and how it can respond to such a crisis. Insolvency offers a chance for recovery through reorganization and debt negotiation, while bankruptcy is a final, inevitable process leading to asset liquidation and business closure.

In conclusion, insolvency and bankruptcy represent two distinct stages of a broader legal process aimed at resolving an entity's financial problems. Insolvency is a temporary state of financial difficulty, while bankruptcy is a final procedure intended for the liquidation of assets and the closure of a business or economic activity. While insolvency may offer an opportunity for financial recovery, bankruptcy implies the loss of control over economic activity and the inability to fulfill financial obligations.

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