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Certain Aspects of Georgian Insolvency Law



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THE THREE LAWS OF GEORGIA ON INSOLVENCY

-  **Enactment of the bankruptcy law in Georgia is related to the collapse of the Soviet Union and transition of the emerging independent states to market economy.**
-  **Georgia adopted the first bankruptcy law only on 8 September 1992. The first law of Georgia on insolvency subsisted for 4 years only but with little effect in reality – it existed on paper only.**
-  **The second law was adopted on 25 June 1996. The law held out and was enforced in practice for 11 years.**
-  **The third and current law was enacted on 15 August 2007 and is in force for about 3 years.**

ASSESSMENT OF FORMER LEGISLATION OF GEORGIA ON INSOLVENCY

- ❖ Previously the main problem was that it was hard to enforce the law into practice.
- ❖ The language of the law was ambiguous and unrefined, often one provision contradicting the other.
- ❖ As a result, Georgian bankruptcy law failed to meet the expectations.
- ❖ Former industrial giants Rustavi Chemical Plant AZOT, Rustavi Integrated Metallurgical Plant, Zestafoni Ferrous Alloy Plant and Kutaisi Automobile Plant and many others fell within the scope of the bankruptcy law.
- ❖ Instead of bankruptcy proceedings, almost all the companies fell to the rehabilitation proceedings.



- ❖ **Unrealistic rehabilitation plans were mapped out to reschedule the debts of the companies. E.g. under the rehabilitation plan, the 115-million-dollar debt of Rustavi Metallurgical Plant must have been paid off in 15 years.**
- ❖ **The 11- year effective period of the second law saw the completion of no bankruptcy case whatsoever – not as single company was bankrupt and not a single company was rehabilitated.**
- ❖ **In June 2005, the second bankruptcy law was amended, as a result of which the bankruptcy manager was allowed to sell the assets of a company at the price enough to pay off personnel salaries and government taxes only.**

- ❖ Newly appointed bankruptcy managers sold the bankruptcy assets (bankrupt estate), putting the entire proceeds towards payment of taxes.
- ❖ E.g. Rustavi Metallurgical Plant that had a 115-million-dollar debt was sold for 22 million US dollars, out of which 60,000 US dollars went towards payment of arrears in wages, and the rest of the money – 21,940,000 US dollars fell to one creditor only – the state.
- ❖ The things got around the same way with Rustavi Chemical Plant AZOT. The company that had a debt of roughly 100 million US dollars was sold for 20 million US dollars, with the state getting the total proceeds.
- ❖ The other creditors for 95 million US dollars in the first case and for 80 million US dollars in the second case got nothing.

NEW LAW ON INSOLVENCY, AIM OF LAW

- ❏ The Law of Georgia on Insolvency Proceedings (the Law) was adopted in 2007;**
- ❏ It seeks equal protection of interests of both debtor and the creditors and provides for specific rules on starting the insolvency proceedings as well as transformation of the case into either bankruptcy or rehabilitation;**

FILING AN APPLICATION INSOLVENCY

-  **Legal ground for filing an application to the court on opening insolvency proceedings is either the insolvency or anticipated insolvency of the debtor;**
-  **Party filing an application on opening the insolvency proceedings has to deposit GEL 5 000 [about USD 3 000] to the court account and pay court fee in the amount of GEL 5 000 [about USD 3 000] ;**

PARTIES ENTITLED TO FILE THE APPLICATION

- 1. Insolvent or expectedly insolvent debtor;**
- 2. Tax and/or customs body in case the debt amounts to at least GEL 50 000 [about USD 30 000], provided that at least 60 calendar days have elapsed since the due date for the repayment of the debt;**
- 3. Creditor if able to present at least 2 (two) court decisions against the debtor upholding claims of other creditors, having already entered into force and being pending for enforcement, provided that joint amount of the debt exceeds GEL50 000 [about USD 30 000];**

- 4. Creditor (creditors) who's claim exceeds 30% of the totally claimed amounts against the debtor according to the latest financial accounting of the latter, provided that at least 30 calendar days have elapsed since the due term for meeting the claim;**
- 5. 2 (two) creditors together, provided that at least 30 calendar days have passed since the due term for meeting each claim, if the claim has not been appealed by the debtor and if the joint amount of the debts exceed GEL 150 000 [about USD 85 000];**

- 6. at least 3 (three) creditors together, provided that at least 30 calendar days have passed since the due term for meeting each claim, if the claim has not been appealed by the debtor and if the joint amount of the debts exceed GEL 50 000 [about USD 30 000];**
 - ❖ Not all creditors can request the opening of the case of bankruptcy.**
 - ❖ The restrictions are set mainly because a creditor with a small claim is not entitled to file for bankruptcy proceedings against the debtor.**
 - ❖ It is obvious that the goal of the law is to make sure that the case of bankruptcy is initiated on a solid basis.**

JURISDICTION

- ✿ Only two courts – Tbilisi and Kutaisi Courts – have jurisdiction over the case of insolvency – the first one for East Georgia and the second one for West Georgia.

APPLICATION FOR INSOLVENCY

Parties entitled to file the application shall notify the debtor in writing 30 (thirty) days in advance regarding the date of filing the application to the court, name of the court, subject matter of the application and its amount.

Once the application is filed, the court shall:

- ✿ decide on accepting the application within 5 days from the date of filing.
- ✿ immediately inform the debtor of receiving the application for opening insolvency proceedings

APPLICATION RECEIVED

- ❖ Once the application is received it is reviewed by the court within 5 (five) days,
- ❖ In case the application is upheld, the court will render a ruling on opening bankruptcy proceedings whereby the court:
 - ❖ appoints the Supervisor/Trustee;
 - ❖ sets the date for the first meeting of creditors (*not earlier than within 30 (thirty) days from publishing the ruling*);
- ❖ The ruling on opening insolvency proceedings has to be immediately published on the board of the court and in official gazette “*Sakartvelos Sakanonmdeblo Matsne*”, where laws are published

LIMITATIONS OVER THE DEBTOR

From the moment the court renders ruling on opening the insolvency proceedings:

- ❧ the debtor is prohibited to conclude any agreement and/or terminate agreements already concluded without prior consent from the Trustee;**
- ❧ each creditor is entitled to present the court its claims within the timeframe established by law (i.e. 30 days from rendering ruling on opening insolvency proceedings), along with indicating the grounds for claiming the debt;**
- ❧ Compulsory enforcement is suspended;**

- ❖ **Securing of debts taken before rendering the ruling, as well as payment of debts and interest rates, penalties and fines (also tax and customs fines) are suspended;**
- ❖ **For the purpose of keeping the enterprise/debtor working, the latter is entitled to take up new contractual obligations, provided that Supervisor's consent is received.**

PARTIES ENGAGED IN INSOLVENCY, BANKRUPTCY AND REHABILITATION

- ❧ Supervisor/Trustee;**
- ❧ Meeting of Creditors;**
- ❧ Conciliation Council;**
- ❧ Creditors' Committee;**
- ❧ Manager of Bankruptcy;**
- ❧ Manager of Rehabilitation;**

TRUSTEE

Supervisor/Trustee is independent, impartial and honest person audit or advocate by profession.

Functions of the trustee include:

- ❏ consideration and assessment creditor and debtor indebtednesses of debtor;**
- ❏ prepare and organize meeting of creditors;**
- ❏ preserve the trusted property and protect it from damages and destruction;**

- ❏ carry out activities related to limiting the usage of the trusted property;
- ❏ ascertain all the creditors and immediately notify them of opening the insolvency proceedings;
- ❏ Trustee is responsible with its property, directly and personally.

MEETING OF THE CREDITORS

- ✦ The first Meeting of the Creditors shall be convened not earlier than within 30 (thirty) days from publishing the ruling on opening insolvency proceedings.**
- ✦ First Meeting of Creditors checks creditors' claims and creates the Conciliation Council.**

Meeting of Creditors reviews and takes decisions on the following:

- ✦ appointment of the conciliation council;**
- ✦ appointment of the Manager of bankruptcy or Manager of rehabilitation;**
- ✦ other issues falling within its sphere of competence;**

CHECKING CREDITORS' CLAIMS

- ❖ **Creditors have to present their claims to the court within 30 (thirty) days from publishing the ruling on opening insolvency proceedings.**
- ❖ **Creditor, having both secured and unsecured claims, is taken as two creditors. All the claims are put in GEL.**
- ❖ **After the deadline for filing claims to the court is passed (i.e. within 30 (thirty) days from publishing the ruling on opening insolvency proceedings), the court shall take decision whether to acknowledge new claim or not.**

CONCILIATION COUNCIL

- ❏ **Conciliation Council is created on the first Meeting of Creditors, after checking of creditor's claims.**

- ❏ **Conciliation Council studies the insolvency of the debtor within a term of 30 (thirty) days, as a result rendering one of the below decisions:**
 - **decision on bankruptcy;**

 - **decision on rehabilitation;**

 - **termination of the insolvency proceedings;**

BANKRUPTCY

- ❖ When put in bankruptcy, an enterprise is managed and represented by the Manager in bankruptcy;**
- ❖ Manager in bankruptcy is appointed by the Meeting of Creditors within 3 (three) days from publishing court ruling on opening bankruptcy proceedings;**

AUCTION

Trusted property may only be sold through the auction.

- ❧ The **first auction** is held on the 30th (thirtieth) day of appointing the Manager in bankruptcy. The auction aims to sell the whole trusted property as one complex with the starting price that is market price of the assets determined by the expert.
- ❧ In case the trusted property is not sold on the first auction, then, on the 30th (thirtieth) day from the first auction second auction will be held. Assets should be sold as one complex with the half price of that, which was the starting price on the first auction.

- ❖ **However within the 7 days from the first auction creditors by majority of votes may decide assets to be sold by piecemeal. Creditors may also decide trusted property to be sold as one complex with its starting price to be not less than the total amount of the claims of first, second, third and fourth rank creditors combined.**
- ❖ **If the trusted property is not sold on the second auction, secured and unsecured creditors may agree to meet the claims of the secured creditors through transferring the collateral to the ownership of the secured creditors.**
- ❖ **In absence of above agreement and within the 60 days from the second auction creditors may also agree to accept the assets in kind or determine other way of selling of assets. Refusal of creditor to accept assets in kind is to be considered as his refusal on its claim.**

- ❖ If within the 60 days from the second auction all creditors refuse accepting assets in kind or if the assets will not be sold in any way, then, bankruptcy case will be terminated and liquidation process of debtor will be initiated.
- ❖ As a result of transferring the property into ownership through the auction, the property is transferred to the new purchaser free of any liens and debts.

RANKING OF CREDITORS WHEN MEETING CLAIMS

- ❏ first rank- procedural costs;**
- ❏ second rank – indebtedness of the debtor arisen after the court renders ruling on opening insolvency proceedings;**
- ❏ third rank – costs and reimbursements related to the appointment of the trustee and carrying out his/her obligations;**
- ❏ fourth rank – all secured claims, including the ones secured as per the tax code of Georgia;**
- ❏ fifth rank – tax indebtedness;**

- ❧ **sixth rank – all other acknowledged unsecured claims;**
- ❧ **seventh rank – creditors' claims presented after the deadline for filing the claims;**
- ❧ **The amount received through the sale of the trusted property is to be disbursed immediately upon ending of bankruptcy proceedings.**

RULES FOR MEETING THE CLAIM

- ❖ Each claim will be met after the claims of the previous rank are fully upheld, unless otherwise unanimously agreed by the creditors. All the claims within one rank are satisfied on an equal pro rata basis.
- ❖ In case the distributable amount is not enough for meeting the claims of one rank creditors, the claims will be met proportionally.
- ❖ Law provides for the opportunity to gain priority in meeting the claims among the same rank creditors as well as the possibility of re-grouping in above rank in case partially dismissing the claims.

RULES FOR MEETING THE CLAIM OF THE SECURED CREDITOR

Unless the mortgage/pledge agreement provides otherwise:

- ❧ if the encumbered thing is sold at a price more than the claim of the secured creditor, the creditor will receive only the amount claimed while the remaining amount will be deposited in the joint claims;**
- ❧ if the selling price of the encumbered thing is less than the claimed amount, the creditor will receive the amount received through the sale of given thing, while the remaining debt will be proceeded as unsecured claim;**

SPECIAL AUTHORITIS OF SECURED CREDITORS

- ❧ After the meeting on checking creditors' claims is held, the question of taking up new debts by the debtor is unanimously decided by the secured creditors.**
- ❧ Secured creditors enjoy the right of suspension of enforcement of the following decisions taken by the creditors:**
 - ❧ essential terms of the agreement concluded with the Manager of bankruptcy and Manager of rehabilitation;**
 - ❧ determination of the timeline for the rehabilitation;**

REHABILITATION

- ❖ **Rehabilitation is managed by the Manager in rehabilitation;**
- ❖ **Timeline for preparation of the rehabilitation plan is set by the creditors, is counted from the date when the court ruling on rehabilitation was published and has to be not more than 60 (sixty) days.**
- ❖ **Rehabilitation plan is reviewed by the Conciliation Council on the 30th (thirtieth) day of publishing the ruling on rehabilitation; the process of review can last for maximum of 10 (ten) days.**

- ❖ **Rehabilitation plan is approved by the secured creditors within 7 (seven) days from receiving the plan from the Conciliation Council.**
- ❖ **For a plan to be approved consent of all the secured creditors is required.**
- ❖ **Rehabilitation plan can be altered in case creditors deem that it is impossible to comply in total or with the part of the plan.**

END/SUSPENSION OF REHABILITATION PROCESS

- ❏ **Rehabilitation ends with the realization of the rehabilitation plan.**
- ❏ **Rehabilitation process is terminated in case the court decides on termination due to the fact that the plan is not complied to. The right of seeking termination of the rehabilitation is granted to each creditor, who's claim is 10%.**
- ❏ **Termination of the rehabilitation plan leads to bankruptcy of the debtor.**

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