About the Policy Spotlight

The Policy Spotlight is a bimonthly publication of the American Chamber of Commerce in Kosovo, which focuses on different economic policies and challenges. The Law on Bankruptcy, adopted on June 2016 is at the focus of analysis for this edition of the spotlight, which aims at explaining the scope of the law and the novelties it brings.

General Overview

Lack of ability of business organizations to fulfill obligations toward creditors is a common problem in Kosovo which is negatively affecting the economic development and contract enforcement. According to World Bank’s Doing Business Report, resolving insolvency remains Kosovo’s weakest indicator, as it ranks 163 out of 189 countries.

Moreover, the report emphasized that there is no insolvency practice in Kosovo, and foreclosure is the only procedure available which takes up to 2 years to complete. Therefore, a well-functioning insolvency system is the key to the survival of healthy and viable businesses, restructuring of those facing with problems and regulation of bankruptcy proceedings of insolvent businesses.

Compared to the previous legislation that regulated bankruptcy proceedings, specifically the Law No. 2003/4 on Liquidation and Reorganization of Legal Persons in Bankruptcy and the Law No. 02/L-115 amending and supplementing the Law No.2003/4 on Liquidation and Reorganization of Legal Persons in Bankruptcy, the new bankruptcy law introduces several new provisions.

First of all, it includes the bankruptcy of debtors as natural persons, which was not the case with the previous legislation. In this regard, the individual debtor shall not be the owner of his assets used for business purposes administered during the bankruptcy proceedings.

Secondly, it defines specific and expedited procedures for Small and Medium Enterprises (SMEs) which are described as business organizations that have an annual turnover up to 1 Million Euros and have up to 25 employees.

Furthermore, with a specific chapter it regulates the cross-border bankruptcy proceedings, which were not covered under the previous law.
Policy Spotlight on the Law on Bankruptcy

Purpose and Scope of the Law

Article 1 of the Law on Bankruptcy, defines the purpose of the law as follows:

Article 1
Purpose
This Law regulates the all matters related to bankruptcy and insolvency of business organizations, provisions for the protection, liquidation and distribution of the assets of a bankrupt debtor to its creditors, and for the reorganization and discharge of debt for qualified business organizations.

Furthermore, this law contains conditions and provisions for initiating and opening a bankruptcy proceeding for insolvent debtors and the conduct of those bankruptcy proceedings.

The scope of this law also covers the legal consequences of the opening and closing of a bankruptcy proceeding, reorganization of a debtor in financial difficulties and the consequences of a discharge of debt for the debtor upon the successful completion of reorganization and liquidation.

Who can become a debtor?

The Law on Bankruptcy applies to all business organizations and specifies that any business organization may be a debtor, including an: individual business, general partnership, limited partnership, limited liability company, joint stock company and branches of foreign businesses.

It should be noted that bankruptcy is a court proceeding. Hence, the Basic Court in Prishtina, Department for Commercial Matters, is authorized for the proceedings and review of the bankruptcy case. A sole judge adjudicates the bankruptcy case. The decision of the Basic Court can be appealed to the Court of Appeals but according to the law the use of extraordinary legal remedies is not allowed.

Initiation of the procedure and opening of a case

There are two different alternatives on how to initiate bankruptcy of a business organization. The first one is known as a voluntary case opened by a debtor where a debtor files either a petition in reorganization or a petition in liquidation.

The other one is known as involuntary case commenced by creditors and it applies for situations when two or more creditors submit a petition to commence a case against an eligible debtor. This petition may be submitted by creditors when:

- debtor has failed to pay at least the debt due to each of the petitioning creditors;
- each debt has been due and payable for at least ninety (90) days;
- total amount of one debt due is at least three thousand (3,000) Euro in amount;
- each debt is not conditional or subject to pending court proceeding or an ongoing arbitration;
- the debtor is generally not paying its debts as they become due, and the total of unpaid debts exceeded five thousand (5,000) Euro.

Petitions for initiating the bankruptcy proceeding must contain at least the following information:

- debtor's name, and all names under which the debtor has conducted business in the last (5) years prior the date on which the petition is filed for bankruptcy;
- debtor's contact information, which at a minimum must include its address, telephone number or numbers, fiscal number, business
registration number, email addresses and any web site address that the debtor has used;

- if the debtor is a legal person (LLC or JSC), all available information regarding officers, directors, shareholders, managers or any other persons with managerial or other control over the debtor's property, along with the contact information for everyone.

As for the petitions filed by creditors, they shall include as many information about the debtor to the extent available to them, but at a minimum shall include the debtor's name and sufficient contact information about the debtor in order for the court to send the notice.

Legal consequences upon opening a case

After filing the petition, the legal consequences of opening a case are as follows:

- creation of the bankruptcy estate;
- conferral of the court with exclusive jurisdiction over the bankruptcy estate and over the debtor;
- automatic imposition of a stay of proceedings against the debtor;
- in a liquidation procedure, removal of the debtor's control overall its property;
- in a reorganization procedure where an Administrator is not appointed or requested, the debtor enjoys all of the rights and duties of a debtor in possession; and
- in a reorganization procedure where an Administrator is appointed, the debtor loses control of all of its property and that control vests in the Administrator.

Pursuant to the Law on Bankruptcy, a petition filed for initiation of bankruptcy procedure shall operate as a stay and injunction, without notice, applicable to all entities.

The stay expires 120 days after the opening of a case, or after the debtor receives a discharge. The stay may be extended beyond 120 days, but only if the court finds that the bankruptcy estate representative has provided sufficient evidence that the extension of the stay would contribute to fulfilment of the purposes under the Law on bankruptcy.

Bankruptcy estate representative

The bankruptcy estate representative is the person who shall take in possession all assets, tangible or intangible, along with all rights, claims or obligations for those assets, of business organization that is subject to bankruptcy proceedings. The bankruptcy estate representative shall:

- administer with all property of the bankruptcy estate;
- have the power to sue and be sued in the bankruptcy estate's name; and
- perform all duties specified in the Law on Bankruptcy for the bankruptcy estate representative.

In a liquidation procedure, the bankruptcy Administrator shall serve as the bankruptcy estate representative. In reorganization procedure, the debtor shall serve as the bankruptcy estate representative when acting as debtor in possession. In reorganization cases where the court appoints a bankruptcy administrator, the Administrator will serve as the bankruptcy estate representative.

Creditors’ Claims

Pursuant to the Law on Bankruptcy, Article 46 on Acceleration of Maturity of All Claims, immature claims shall be considered as mature ones when the court decides on the opening of the bankruptcy case. So, any interest of any form will be terminated upon
the opening of the bankruptcy case and the entire amount of the loan shall be considered payable at that moment.

There are two types of creditors’ claims: secured and unsecured claims. A claim is considered a secured claim only to the extent of the value of the collateral securing its repayment. If the creditor’s claim exceeds the value of the creditor’s collateral that ensures the payment of the claim, the creditor holds an unsecured claim.

Each creditor must file a proof of claim with the court to establish the validity and amount of its claim.

In a liquidation case, the creditor must register the claim in accordance with this Article within 60 days from the date the notice for opening the bankruptcy proceeding has been received.

In a reorganization case, unless the court orders otherwise according to the needs of the reorganization, a creditor must register the claim within 30 days from the date of receiving the notice for opening the bankruptcy proceeding.

The payment of creditors’ claims

The first claims paid are the secured ones, followed by unsecured claims. All unsecured claims are presumed to have the same priority for purposes of distribution. Priorities of payment of unsecured claims are prioritized as follows:

1. administrative expenses (all expenses for the administration of the case, including payment of the administrator and practitioners);
2. claims deriving from domestic relations and restitution of victims;
3. claims deriving from employment relationship;
4. tax claims; and
5. any other unsecured claims.

The Administrator (an entity appointed as the representative of the bankruptcy estate) shall consider the payment of administrative expenses with priority.

Reorganization and Liquidation

The Law on Bankruptcy provides two types of proceedings: Reorganization and Liquidation

Reorganization as defined by the law is the process by which the financial well-being and viability of a debtor’s business can be restored, jobs preserved, and the business continues to operate. Reorganization may be applied in different forms, including debt forgiveness, debt rescheduling, debt-equity conversions and sale of the business or parts of it as a going concern.

The law reads that a case involving an SME debtor shall be in all respects treated as a reorganization case. In each case, the SME should file a reorganization plan within 30 days after the initiation of bankruptcy proceeding. In this regard, the law recognizes the notion of monitor who is appointed by the court when the debtor is an SME, and his role is to advise the debtor with regard to business, perspectives of business, and the reorganization plan which will be accepted/confirmed by all creditors.

On the other hand, liquidation refers to the proceedings designed to sell and dispose of the debtor’s property, assets and wealth for distribution to creditors. This happens when the debtor cannot find a way to be recovered and chooses the final step before the discharge of the debtor, in which case the business organization ceases to exist.

The court appoints an Administrator no later than 3 days, in the following cases:

- after the filing of a liquidation case by a debtor;
- after the opening of a liquidation case following the filing of a bankruptcy petition by creditors;
- after the conversion of reorganization into liquidation;
• after the court decides to remove the debtor in possession or a serving Administrator

Discharge from debts and closing of the case

A discharge shall mean paying off debts and according to the Law on Bankruptcy, it:
• avoids any judgment obtained at any time, judgment that determines the full personal liability of the debtor with respect to any claim, for which the debtor has requested discharge;
• has the effect of a final court decision and operates as an injunction and prohibition against the commencement or continuation of any action or proceeding of debtor regarding debt collection, debt recovery or any such claim for compensation, regardless if the debtor has personal liability toward such claim.

A debtor shall receive a discharge of all claims that existed until:
• the moment of confirmation of the reorganization plan; and
• the moment the liquidation case has been completed or the notification has been sent to the business registration agency and tax administration on case completion, depending on which of these occurs last.

An individual debtor (as individual business or partnership member) is excluded from debt discharge respectively any of the following:
• claims not related to the debtor's business activity;
• domestic relations claims;
• claims arising from restitution of victims;
• tax claims accrued for the period of 1 year from the day of the opening of the case;
• claims not listed in the list of claims;
• claims for which the creditor has not received a regular notice and as a result could not file to the court the claim and proofs on time;
• claims that have arisen as a result of debtor's fraud;
• claims that have arisen as a result of the debtor's breach of a duty for good trust; and
• claims that do not result from contracts but that have incurred as a result of the intentional injury caused by the debtor to another entity or to the property of another entity.

Cross-Border Bankruptcy

The Bankruptcy Law has a specific chapter for Cross-Border Bankruptcy applicable for foreign business organizations and their branches in Kosovo.

This chapter applies when:
• a foreign court or a foreign representative of bankruptcy estate seeks assistance from the competent court in Kosovo regarding the foreign bankruptcy proceeding;
• assistance is sought in a foreign state in connection with a proceeding under this Law;
• a foreign proceeding and a proceeding under this Law in respect of the same debtor are taking place concurrently; and
• creditors or other interested persons in a foreign State have an interest in requesting the commencement of, or participating in, a proceeding under this Law.
Conclusion

The new Law on Bankruptcy improves the commercial legislation in Kosovo by establishing a contemporary system for bankruptcy procedures, a practice which couldn’t be applied in the past due to lack of legal provisions.

Furthermore, in addition to businesses using the new bankruptcy legal framework, it is necessary for courts to accurately enforce provisions of the new law, thus enhancing trust of domestic and foreign investors.

As there is no developed practice by the courts and bankruptcy is not seen as a suitable remedy for creditors nor debtor, we should work on the capacity building of the courts, the administrators and all the relevant institutions in order to enhance the legal security for parties entering into bankruptcy.

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