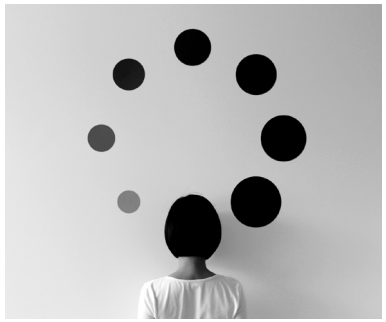
A&O SHEARMAN

Restructuring across borders
Bulgaria

CORPORATE RESTRUCTURING AND INSOLVENCY PROCEDURES | JANUARY 2024

Contents



Introduction

Bulgarian corporate insolvency law is almost entirely governed by Part IV of the Commerce Act 1991 (the **Commerce Act**), which entered into force in 1994. Separate insolvency regimes apply to commercial banks, insurers, and public enterprises that exercise a State monopoly or are created by a special law.

Since 1994, Part IV has been amended on numerous occasions. In 2010, amendments were made to the Commerce Act (some of which took effect from 1 January 2011) to enhance the position of secured creditors and to tidy up the drafting of some of the insolvency rules. In March 2011, amendments concerning the protection of the debtor's employees in the event of insolvency were made to the Commerce Act. Amendments to the Commerce Act were made in 2013, aiming to increase legal certainty and protect creditors' interests by introducing changes to the clawback rules. The most recent (substantive) amendments were made at the end of 2016, effective as of 1 July 2017, to introduce a new Part V of the Commerce Act – Stabilisation procedure (*Част пета от Търговския закон - Производство по стабилизация на търговец*) applicable to companies facing financial difficulties. The amendments envisage measures to prevent the opening of insolvency proceedings of a company through reaching an agreement between the company and its creditors on how t he company's debts will be restructured and repaid.

The Bulgarian corporate insolvency procedure contained in Part IV of the Commerce Act is an example of a single-entry, multiple-exit insolvency procedure.

Under Bulgarian law there are the following principal regimes for companies in financial difficulty:

- Part IV Commerce Act insolvency procedure (*Част четвърта от Търговския закон – Несъстоятелност*), which arranges:

  (i) voluntary solvent liquidation; and

  (ii) forced court liquidation on public policy grounds;

- informal out of court arrangements;
- enforcement of security by a secured creditor; and
- Part V Commerce Act – Stabilisation procedure (*Част пета от Търговския закон - Производство по стабилизация на търговец*).

Part IV Commerce Act insolvency procedure

(Част четвърта от Търговския закон – Несъстоятелност)

This is a single entry, multiple-exit insolvency procedure. It is commenced by filing a petition to the competent court. How it will continue and end depends on whether the insolvent company has enough assets to cover the initial expenses of the procedure and whether, in the course of the insolvency procedure, a restructuring plan is proposed.

The possible exit routes from the procedure are as follows:

- The insolvent debtor may be declared insolvent, its commercial activities terminated, all its assets attached, and the winding-up procedure stayed for lack of assets to cover the initial expenses of the procedure (Art. 632, Commerce Act). Where the debtor has insufficient assets to cover the initial expenses, the court will invite the creditors (or other petitioners for insolvency) to fund those expenses. If they do so, the procedure will continue as described below. If they do not fund the expenses, the court will stay the insolvency proceedings. Within one year of the court staying proceedings, the proceedings may be continued where the debtor or a creditor provides funding for the initial expenses. If that does not happen, the court will close the insolvency proceedings and remove the debtor from the commercial register.
- The insolvent debtor may be declared insolvent, and the winding-up procedure commenced, followed by the appointment of a "syndic" (синдик) and the ascertaining of the creditors and the assets of the insolvent debtor. This route is likely to continue in one of the following ways:
  - a proposal to the court and approval by the court of a restructuring plan (Arts. 696+709 Commerce Act) (a formal rescue);
  - the realisation of the debtor's assets and the payment of the debtor's creditors in accordance with the priority provisions of the Commerce Act (in cases where no restructuring plan has been proposed, or the proposed plan has not been approved by the court (Arts. 710+739 Commerce Act)) (a bankruptcy); or
  - an out-of-court arrangement with all creditors (Arts. 740-741a Commerce Act), which could happen in all stages of the insolvency proceedings (an informal rescue).

In all cases, the court will hold a final decision formally closing the insolvency proceedings.

Informal out-of-court arrangements

An insolvent debtor and some or all of its creditors (whose claims have been accepted by the syndic) may enter into an informal out-of-court arrangement. Even if such arrangements were collective (in the sense that they were for the benefit of all creditors), they would be entered into informally and governed by contract rather than insolvency law. If the debtor failed to live up to its promises to the creditors, the creditors would only have contractual remedies against the debtor.

However, arrangements entered into by some (not all) of the existing creditors may be declared null and void under the provisions of the Commerce Act if the arrangement is detrimental to the creditors which are not party to the out-of-court arrangement.

Voluntary solvent liquidation

A company's shareholders or a partnership's partners may decide to wind up the company or the partnership voluntarily. Provisions to this effect are contained in relation to each type of partnership or company in Part I of the Commerce Act. It is a condition of commencing such proceedings that the company or partnership is solvent.

If the liquidator appointed in a solvent liquidation discovers that the company is, in fact, insolvent, the liquidator is required to file a petition for the commencement of formal insolvency proceedings under Part IV of the Commerce Act.

Forced court liquidation on public policy grounds

Several public policy grounds may result in a forced court liquidation of a company. For example, grounds include, among others: (i) the illegality of activities of the company or the partnership; (ii) the request of the minority shareholders or partners for winding up in exceptional circumstances; and (iii) there being no appointed management for a certain period.

Provisions to this effect are contained in relation to each type of partnership or company in Part I of the Commerce Act. In this case, if the company is solvent, it will enter into a forced solvent liquidation rather than insolvency proceedings.

Enforcement of security by a secured creditor

In Bulgaria, mortgages and possessory pledges are enforced through a court foreclosure procedure which requires the sale of the secured assets through a public auction supervised by a state or private court bailiff. Commercial possessory pledges and registered pledges may be enforced through an out-of-court foreclosure procedure under which the secured creditor may sell the secured assets by private contract without the involvement of a bailiff (provided certain conditions are met). These procedures are, by their nature, non-collective in that they aim at satisfying a single secured creditor.

Part V Commerce Act – Stabilisation procedure

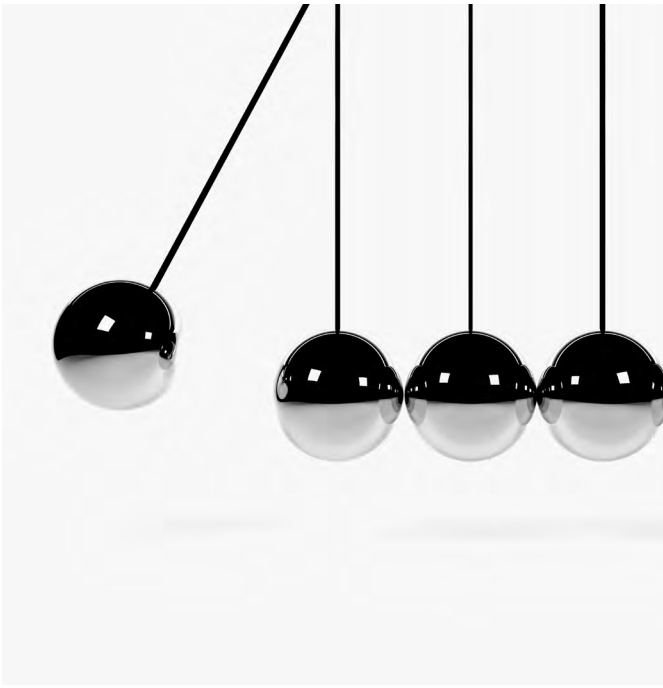
(Част пета от Търговския закон – Производство по стабилизация на търговец)

A stabilisation procedure may be opened in respect of a company, which is not insolvent, but under an imminent threat of insolvency. An imminent threat occurs where the company would, within six months of the date of filing the stabilisation petition, be unable to pay its debts or is likely to stop paying them. The stabilisation procedure is not available for banks, insurance companies and some public undertakings.

A petition to open a stabilisation procedure may be filed with the court, but only by the debtor and not by a creditor. The petition must contain, among other things, a detailed stabilisation plan with a specific proposal on the manner, time limits and conditions for repayment of the company's creditors. Participants in the stabilisation proceedings are all creditors of the company.

If the court establishes that the required grounds exist, it will open a stabilisation procedure, appoint a trustee (to supervise the activity of the company, support the company and the creditors in clarifying the proposed stabilisation plan, etc.) and, if necessary, appoint an auditor (to report to the court and the creditors on whether the stabilisation plan corresponds to the financials and property of the company).

The court may impose an attachment or other security measures and will schedule a court hearing. The plan is then voted on by the creditors and approved or rejected by the court. If approved, the plan becomes mandatory for the company and its creditors.



European Insolvency Regulation

The EU Regulation on Insolvency Proceedings 2015 (Regulation (EU) 2015/848) (the **Recast Regulation**) applies to all proceedings opened on or after 26 June 2017. Its predecessor, the EC Regulation on Insolvency Proceedings 2000 (Regulation (EC) 1346/2000) (the **Original Regulation**), continues to apply to all proceedings opened before 26 June 2017. One of the key changes in the Recast Regulation is that it brings into scope certain pre-insolvency "rescue" proceedings, which are now listed alongside the traditional insolvency procedures in Annex A to the Recast Regulation.. The Recast Regulation retains the split between main and secondary/ territorial proceedings, but secondary proceedings are no longer restricted to a separate list of winding up proceedings - secondary proceedings can now be any of those listed in Annex A. By contrast, the Original Regulation listed main proceedings in Annex A and secondary proceedings (which were confined to terminal proceedings) in Annex B.

Of the above restructuring and insolvency regimes, only the Part IV Commerce Act insolvency procedure (*Част четвърта от Търговския закон Несъстоятелност*) was available as a main proceeding under the Original Regulation.

The Part IV Commerce Act insolvency procedure was also available as a secondary proceeding under the Original Regulation. It remains to be seen whether the only exit route available as a secondary proceeding under the Original Regulation would be bankruptcy (rather than a formal or informal rescue).

Under the Recast Regulation, only the Part IV Commerce Act insolvency procedure (*Част четвърта от Търговския закон – Несъстоятелност*) is listed in Annex A.

Currently, Part V of the Commerce Act – Stabilisation procedure (*Част пета от Търговския закон - Производство по стабилизация на търговец*) is not listed in Annex A.

Finally, while the Bulgarian Government has prepared draft legislation transposing the requirements of Directive (EU) 2019/1023 of the European Parliament and the Council of 20 June 2019, said draft is yet to be submitted to the Bulgarian Parliament for consideration. Submission may not happen any time soon, given the political uncertainty in the country and the high likelihood of a general election in the autumn of 2022.

Key contacts

If you require advice on any of the matters raised in this document, please contact any of our partners or your usual contact at A&O Shearman, or email **rab@aoshearman.com**.

This factsheet has been prepared with the assistance of Spasov & Bratanov Lawyers' Partnership. Any queries under Bulgarian law may be addressed to the key contacts listed below:

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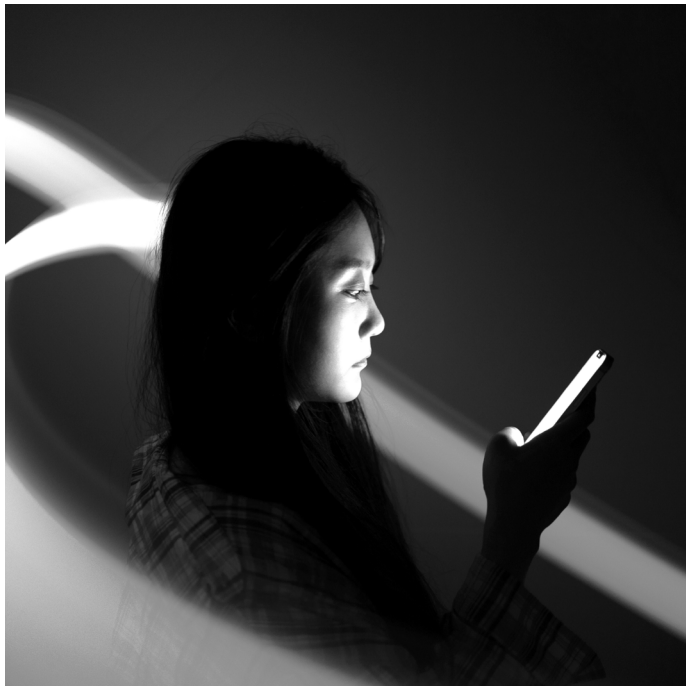
Further information

Developed by A&O Shearman's market-leading Restructuring group, "**Restructuring Across Borders**" is an easy-to-use website that provides information and guidance on all key practical aspects of restructuring and insolvency in Europe, Asia, the Middle East and the U.S.

To access this resource, please **click here**.



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