

CONSIDERATIONS ON THE MEASURES TO COUNTER THE RISK OF BANKRUPTCY FOR SMES DURING THE FINANCIAL CRISIS

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The financial crisis in Romania has expressed in an eloquent manner and meant large negative effects, such as external factors generated by trigger of the financial crisis in Romania in October 2008 and internal factors for society that fundamentally influenced the decreasing of funding in 2009.

Promotion of private initiative is, in our opinion, one of the methods that attenuate the financial effort of state for social segment which generates costs and, is producing revenue for the state. In this paper we promote the idea of opening a fundamental process of restructuring the SME's management mentality, that of safeguarding of the enterprises with existing instruments, but also with new proposals to the Government, for regeneration as soon as possible of the country's economic and human factors capable of working.

Keywords: bankruptcy, SME, Reorganization, companies, crisis, fusion.

JEL code: G - Financial Economics. G01 - Financial Crises.

1. The influence of internal and external factors on financial indicators in 2009

-Global economic recession has affected all Romanian companies, from largest to smallest. Moreover, access to the funds that the bank could provide for business was locked by the state. Basically, through the Ministry of Finance which borrowed from private banks almost all the money from market to pay salaries and pension budget, the Government, indirectly, locked the national economy. Thousands of companies throughout the country unreasonably have long waited the repayment of VAT to which they were entitled, and that the financial taxation delayed to make it, deadlines being exceeded with months. Instead, for every invoice issued, but not received, the state further requires for firms to pay VAT de-capitalising them and pushing them towards bankruptcy. Establishing flat tax to be paid even by companies which were not registered profit, has determined in 2009, that 120.509 companies to suspend its activities.

-Currency depreciation; it equaled or exceeded the substantial discounts of cars sellers that showed discounts and promotional prices about 30 - 40%.

-Transactions with new cars had a significant rebound, and volumes were decreases of 50% or even 60% compared to the same period last year, some car dealers being forced to close their showrooms and to lay off some employees.

-Romanians real income levels have been affected by currency depreciation: those who had paid rates have experienced the strongest rate shock. Payment amounts were not to be neglected, the rates increased from one quarter to another and even 30%, while nominal revenues remained constant or even declined in condition of rising unemployment. This could lead only to overdue and late payment, short-term liquidity problems, increasing leases terminated, an influx of requests to reschedule the payment obligations.

-Decrease of the credit line

2. Financial crisis outside Romania

Except Poland, where the number of bankruptcies in the first nine months of 2009 remained below 1.000, in all other countries, the recession has felled many SMEs. Romania is by far the most affected, given that in the first six months of 2009, over 100.000 SMEs went into bankruptcy, from a total of 600.000 registered at the ministry.

Germany. German SME's bankruptcies mean problems for Europe. Germany's economic recovery could slow because more and more midsize companies - the skeleton of industry - can not face with market's conditions and bankruptcy. This situation has a negative impact on euro area, under the condition in which, according to The Wall Street Journal, Germany, has the largest economy on the continent³³³.

In **Poland**, 497 companies have declared bankruptcy in the first nine months of the year 2009 compared with 317 during the entire 2008, according to Coface, the credit insurer. In the first half of 2009 the SME sector has been hit by falling demand and by the tighter credit conditions.

In **Hungary**, SMEs have been affected by evaporation of demand and by reducing the access to financing, but unlike Poland, the current situation shows no improvement. Industrial production continues to be 20% lower than in 2008, and SMEs production has fallen by a fifth.

In the **Czech Republic**, 6591 entities (companies and individuals) were asked in the first nine months of 2009, the reorganizing under bankruptcy protection, up 70% compared to last year. 58% of all complaints are made by companies, according to Creditreform, credit agency. Czech Union of SMEs said that access to credit is the main problem with which is facing the sector. Lack of funding leads to postponement or cancellation of investment plans.

3. The situation of economic crisis in Romania

Usually the financial crisis means an economic environment that is characterized by an acute lack of liquidity, which goes to more expensive credit bank. In Romania the beginning and end of crisis is marked by certain indicators that presented in Fig. no. 1.

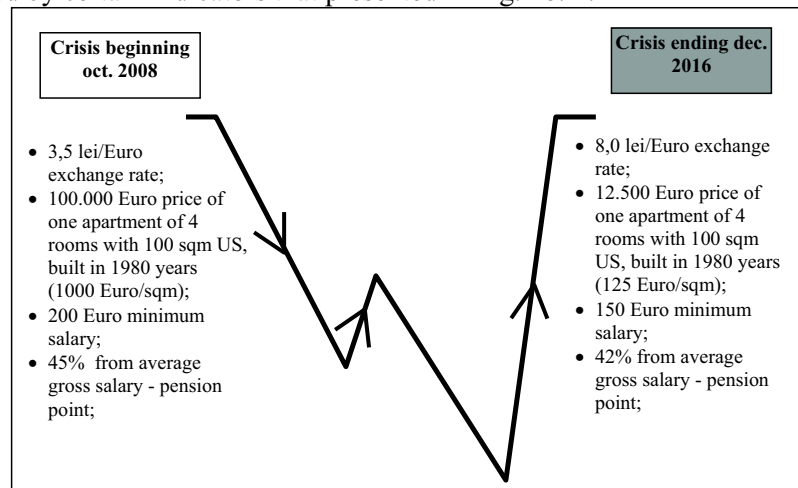
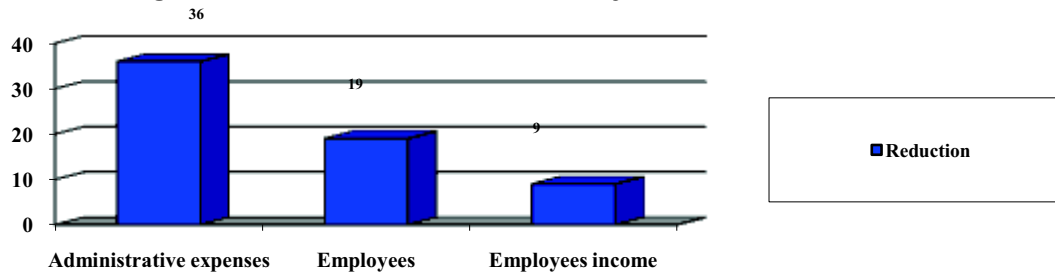


Fig. no. 1. Features of the financial crisis in Romania

In **Romania**, 90% of SME's are affected by economic and financial crisis, difficult economic situation leading to increased number of bankruptcies. Among the measures that companies have taken to decrease the impact of economic crisis, 36% of them have reduced administrative costs, 19% have reduced the number of employees and 9% have reduced the income of employees, as represented in the chart below.

³³³ <http://www.zf.ro/business-international>.

Fig. no. 2. Anticrisis measures taken by Romanians SME's



Year 2010 has not yet good signs for Small and Medium Private Enterprises in Romania. Last year alone, over 190 thousand SMEs and authorized individuals have ceased. Specifically, we present in table from below, cases that favor bankruptcy and measures to avoid bankruptcy, some of them being even proposed by SME and NCPSMER (National Council of Private Small and Medium Enterprises in Romania), as measures for the economic crisis.

Causes that promote SMEs Bankruptcy	Measures to avoid SME's bankruptcy
<ul style="list-style-type: none"> -Depreciation of national currency. -Lower transaction with cars. -Decrease real estate transaction. -Reduce your credit line. -Reduced access to financing and funding hinder. -High costs of interest. -Exports decline. -Low income. -Increasing the CAS's costs. -Introduction of minimum tax. -Sales decrease. -Price increases. -Incapacity of paying. -Entering into insolvency. -Declining real incomes of Romanians. 	<ul style="list-style-type: none"> -Reducing costs through layoffs. -Employee salary reduction. -Reducing administrative costs. -Icing liquidity. -Simple bookkeeping and halving the tax on buildings³³⁴. -Allocating of minimum 0.5% of GDP for the foundation and development programs for SME's³³⁵. -Widespread of the absence of taxation of reinvested profits and reinvested dividends. -Ministry of SMEs of programs on an emergency immediately after the 2009 budget approval. -VAT payment when goods are delivered, services are rendered or works are executed. -Elimination of abusive controls on companies. - Encouraging exports through subsidies. -Creating Counter-Guarantee Fund of the credits in the first half of 2009. -Significant and urgent reducing of extra-taxation. -Simplification of procedures for accessing structural funds and increasing access to consulting services in this area³³⁶.

4. Anti-crisis measures taken by Government

³³⁴ <http://www.financiarul.com>, April 1th, 2010.

³³⁵ <http://www.newschannel.ro/stiri/masuri-anti-criz-a-pentru-imm-uri>.

³³⁶ Idem.

Boc government took steps that led to the cancellation of firms. By eliminating the taxation for microenterprises with 3% of incomes, Boc government put most common obstacle to self-employment solutions. In addition, by introducing flat tax, hundreds of thousands of small companies, generally with a single employee, were closed.

Also, there are many companies that are in bankruptcy, but have not yet said so. Many require judicial protection, asking for insolvency, to be safe from creditors.

Among **crisis measures** already taken by the Government is allocating the largest share of GDP over the past 20 years, for investment, facilities for hiring unemployed and purchase of nearly 17.000 homes through "First Home" program.

Continuing Rabla program, building houses for rural specialists, rehabilitation of thermal and county road blocks, First Silo Program, NHA housing selling to tenants, supporting SMEs and local authorities which are accessing EU funds by providing state guarantees and technical unemployment are other measures already taken by the Government and presented by Emil Boc.

Among the measures to support businesses, the premier noted reinvested taxed profits, deferred payment of outstanding obligations, accelerating tax refund, state aid, incentives for energy and chemical industry, reducing taxes and tariffs parafiscal. Among crisis measures, Emil Boc recalled including VAT at 19% and maintaining a flat at 16%³³⁷.

But all these measures seem not to be the best and not sufficient for the effective exercise of SMEs because, due to other measures adopted by the Government such as the introduction of flat tax, there are favorable conditions for progress.

5. Considerations on anti-crisis measures

Experts say the biggest problem of business is restricted access to credit, and bad news is that banks will not finance companies resumed in 2010, because it will analyze the situation of companies which will seeking loans on the balance sheet situation of 2009, which "looks disastrous."

On the other hand, banks have their own reasons to think twice before approving a loan. In 2009, arrears over 90 days were recorded in loans, over three times higher than in 2008 and represented 75% of all amounts due.

Neither in terms of tax payment obligations to the state, companies did not do better. Experts recommend to the companies with debts of more than 30 thousand lei and debts to the budget over 30 days, to avoid insolvency and forced execution by preventive composition with regulated by Law 381/2009. Preventive composition is an amicable settlement between the debtor and creditors that hold at least two thirds of the value of receivables.

5.1. How to put protected from insolvency?

According to the law, insolvency or bankruptcy of the debtor's assets are characterized by insufficient cash funds available to pay outstanding debts.

It is considered that it may declare bankruptcy when the debtor, after 30 days in arrears, has not paid its debt to one or more creditors. Bankruptcy is imminent when the debtor proves that it can not pay at maturity, outstanding debt incurred with the funds available from the due date.

For companies trying to save his business, the next step is the **process of reorganization**.

6. Reorganization - measure against bankruptcy risk for SMEs

In the current economic situation is expected as part of economic agents continue to encounter difficulties in activity and even to go insolvent.

³³⁷ Source: Wall-Street.ro.

Unfortunately, most of those traders who go into insolvency, unnecessarily are trying to recover the activity of society through their own efforts, without resort to specialized consultants in the field and without the use of legal provisions designed just for protection. Such attempts of recovery leads mostly with a failure, so that society finally comes to bankruptcy, without any possibility of economic recovery.

Law no. 85/2006 of insolvency ("Insolvency Law") specifically provides judicial reorganization, as a extent of recovery of economic activity of a company in a state insolvency or in impending insolvency, being real chance of recovery and continuing a business that normally would be under bankruptcy.

6.1. Reorganization procedure in the Romanian legislation

Unlike the laws of other states, Romanian legislation does not regulate the judicial reorganization procedure, which still can not remove a conventional reorganization. This method of reorganization involves, in practice, debtor negotiations with major creditors on rescheduling the debt payment, but in such a procedure the debtor has no legal protection³³⁸.

Judicial reorganization, aim the "redressing of the debtor and payment of liabilities in terms of restructuring the company and its activity"³³⁹, and saving in this way, a company in default, but still viable.

Judicial reorganization is triggered by an application for entry in insolvency which the debtor in insolvency or in a state of imminent insolvency or a creditor, submit to the Court. In this application the company must accompany the several pieces, among which the declaration by the debtor and shows its intention to enter into the reorganization procedure.

After introducing the application and verification of documents submitted by the debtor, if the legal requirements are met, the judge will order the opening of the general procedure. By this decision to initiate proceedings, the judge will appoint an judicial administrator. To qualify the reorganization procedure it must be proposed such a plan by the debtor, by the judicial administrator or by the creditors. **The plan should contain concrete ways to restructure the company, which may take the form either the debtor's restructuring and continuing future business or liquidation as part of the debtor, or a combination of two previously proposed methods.**

Reorganization of the company closes when you have met all payment obligations assumed by the reorganization plan.

6.2. Advantages of entry into reorganization proceedings

There are several advantages of opening the reorganization procedure for a company in difficulty, such as:

- From the date of opening of the reorganization law there **are suspended all judicial or extrajudicial actions** aiming to achieve claims against the debtor or his property. Thus, under art. 36 of Law no. 85/2006, the law suspended all judicial or extrajudicial actions to achieve the claims against the debtor or his property, so that no creditor can no longer operate separate companies in insolvency proceedings to recover his claim. Also under this article there are suspended any levy of execution or attachment of company accounts. All payments made during the insolvency proceedings will be made by a single bank account, which can not be stopped.

- **No longer pay outstanding debts than under a reorganization plan without paying interest or penalties.** From the opening of proceedings, under art. 41 of Law no. 85/2006, no interest rate, increase penalty or charge will not be added to claims arising, prior to the opening of proceedings

³³⁸ <http://www.avocatnet.ro>.

³³⁹ Csaba Bela Nász – The opening of insolvency procedure, C.H.Beck Publisher, Bucharest, 2009, pag. 42

(excluding guaranteed debt). Thus, by stopping the flow of interest and penalties, it is prevented the increasing liability company.

- The possibility of **rescheduling payment of debts** by creditors, etc.
- The company that was willing to open insolvency proceedings may be subject to judicial reorganization under a reorganization plan, through which can be obtained in certain circumstances or may even require, rescheduling of payments to creditors during the reorganization, which may take up to three years, with possibility of extension for another year.
- In judicial reorganization, the debtor business is conducted by a special administrator named by the company management, who may even be the administrator. Thus, leadership activities of the debtor may remain in the hands of the debtor's former management bodies, which are best placed to continue the company's activities. Their work is supervised by the judicial administrator.
- According to art. 77 of Law no. 85/2006, applications for the recovery procedure or other rights shall be exempt from stamp duty, which is an advantage in making steps to recovery.
- In the judicial reorganization, the company operates on the principle "business as usual", remaining an economic market player, and can keep customer brand and heritage.
- During insolvency, the company does not pay and does not charge VAT.

7. Mergers - another measure to counter the risk of bankruptcy during the crisis

Fusion is a "technical and legal process through which the restructuring of companies is done"³⁴⁰, when two or more companies come together to form a single society. Fusion brings benefits related to strengthening of the company's market, getting a larger share local market or even expansion into other geographic regions. Another advantage of fusion is related to business saving and personnel rescue in conditions of market competition and its impact on business. Vertical integration of business is another benefit of the fusion, so that it shortens the chain of production and distribution. For example, a furniture manufacturer may purchase a wood supplier to eliminate the problem of raw material acquisition. Because it will be reduced certain costs, it will increase company's profits. Another advantage of the fusion is diversifying its product portfolio by launching its own range or buying a player that already offers that product. Fusion also offers an advantage in terms of taxation.

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