The Insolvency Law of Central and Eastern Europe

Twelve Country Screenings of the New Member and Candidate Countries of the European Union and Russia: A Comparative Analysis

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VII. Lithuania

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5. Summary and Perspectives

1. Introduction

a) Historical Background

Within a relatively short period of time the Republic of Lithuania adopted three main editions and amendments of the Enterprise Bankruptcy Law (EBL). The first EBL entered into force on 15 October 1992 (EBL 1992),[309] the second on 1 October 1997 (EBL 1997)[310] and the third and current one on 1 July 2001 (EBL 2001 or EBL).[311]

In comparison to the EBL 1992, the scope of application was widened by the EBL 1997 to encompass all enterprises, public institutions, banks and credit unions registered in Lithuania. This was maintained by the EBL 2001.[312] However, restructuring/rehabilitation of enterprises were excluded from the EBL and regulated in a Law on Restructuring of Enterprises (LRE) which also came into effect on 1 July 2001.[313] By creating a separate set of rules and procedure for the restructuring of enterprises, the legislator aimed at improving the information related to enterprises "experiencing temporary financial difficulties" and at increasing the chances for such enterprises to avoid bankruptcy and to regain competitiveness.[314] The main objective of the EBL 2001 was to address

[309] Lietuvos Respublikos įmonių bankroto įstatymas. Valstybės žinios, 1992, no. 29-843. Available also in English at http://www.lrs.lt/ (visited: 30 August 2007).

[310] Lietuvos Respublikos įmonių bankroto įstatymas. Valstybės žinios, 1997, no. 64-1500. Available also in English at http://www.lrs.lt/ (visited: 30 August 2007).

[311] Lietuvos Respublikos įmonių bankroto įstatymas. Valstybės žinios, 2001, no. 31-1010. Available also in English at http://www.lrs.lt/ (visited: 30 August 2007). Note that the available English version is not always up to date.

[312] However, specifics for certain debtors (e.g. banks) may be regulated in other laws, cf. below 2 b).

[313] Lietuvos Respublikos įmonių restruktūrizavimo įstatymas. Valstybės žinios, 2001, no. 31-1012. Available also in English at http://www.lrs.lt/ (visited: 30 August 2007). Note that the available English version is not always up to date.

[314] Art. 1 para. 1, 2; Aldona Garškienė, Kristina Gaškaitė, Enterprise Bankruptcy in Lithuania, Journal of Business Economics and Management 2004, vol. V, no. 1, pp. 51, 57.

the increase in numbers of bankrupt enterprises, the late filing of petitions for the institutions of bankruptcy proceedings and the long duration of bankruptcy procedures.[315]

Certain aspects of insolvency proceedings[316] can be found in the Civil Code (CC)[317] and Code of Civil Procedure (CCP)[318] and other laws.

b) Insolvency Practice

Since the first introduction of the EBL in 1993 till 1 July 2006 4,910 companies have gone bankrupt, i.e. 1.4% of all registered companies. The number of newly instituted bankruptcies rose steadily. After a decline in 2003 the number rose again, e.g. by 9% from 2004 to 2005. In the first half of 2006, 404 new bankruptcies were initiated. Until July 2006, the proceedings concerning 4,712 enterprises started in court while 198 enterprises were subject to extrajudicial bankruptcy procedures. Most bankrupt companies were wholesale and retail (41.2%) and manufacturing (27.6%) companies. So far, the proceedings of 3,578 enterprises have been finished, while the others are still pending. Three enterprises have been reorganised and 14 have been rehabilitated.[319] Regarding the length of bankruptcies, several statistics can be found. The

[315] Garškienė, Gaškaitė, p. 57 and with statistics on the development of bankruptcies between 1992 and 2001 at pp. 52-57.

[316] In this article, the term „insolvency proceedings" has a wide meaning encompassing the norms in the EBL, the LRE as well as related norms in other laws.

[317] Lietuvos Respublikos Civilinis kodeksas Valstybės žinios, 2000 no. 74-2262. Available also in English at http://www.lrs.lt/ (visited: 30 August 2007). Note that the available English version is not always up to date.

[318] Lietuvos Respublikos civilinio proceso kodeksas. Valstybės žinios, 2002, no. 36-1340. It is not available in English.

[319] All numbers are provided by the Department of Enterprise Bankruptcy Management (hereinafter DEBN) and published on its website www.bankrotodep.lt. Similar, see also "Insolvenzen in Europa 2006/2007" by Creditreform, available at: http://www.creditreform.de/Deutsch/Creditreform/Presse/Creditreform_Wirtschaftsforschung/Insolvenzen_in_Europa/Ausgabe_2006-07/Insolvenzen_Europa_2006_de.pdf (visited: 30.8.2007), at pp. 25-27. According to this study, Lithuania saw an increase of insolvencies by 4.5% between 2005 and 2006.

following numbers are provided by the DEBN: in 40% of all cases procedures take two years, in 30% they take three years. 6% of the bankruptcies opened in 2002 where closed within one year. In the first half of 2006, 3% of all new bankruptcies were closed within that period. A recent survey conducted by the World Bank[320] in the year 2006 comes to the result that on average it takes 1.7 years to resolve a bankruptcy. According to that survey, Lithuania has a recovery rate of 50.5% which is better than those of its Baltic neighbours (34.8% in Latvia and 39.9% Estonia) but worse than the OECD average of 74.0%. The costs (7.0% of the estate) are nearly on OECD average (7.1%).

The main reasons for the insolvency are the following: (1) inefficient use of the production capacities as well as fuel, energy resources, local raw materials and other material resources; (2) inactivity of the management bodies of companies and their reluctance to take measures to solve the problems by reorganising the company; (3) inability of enterprises to adapt themselves to market conditions; (4) insufficient control of the financial accounting of companies; (5) slow reorganising of large companies.[321]

c) Objectives and Status of Reforms

Amendments to the EBL 2001 introduced for the first time a simplified bankruptcy process (cf. Art. 2 para. 13 and Art 13[1] EBL), a two-stage satisfaction of creditors' claims and priority satisfaction of secured creditors (see Art. 34 et seq EBL). However, already the draft law of the current EBL was criticised, e.g. by the Lithuanian Free Market Institute, i.a., because of the proposed insolvency criteria, provisions on the institution of bankruptcy proceedings as well as the sequence of satisfying creditors' claims.[322] After more than six years of practical experience, the EBL and LRE today face heavy criticism from insolvency practitioners

[320] The Doing Business Project. http://www.doingbusiness.org/Explore Economies/?economyid = 114 (visited: 30 August 2007).

[321] Garškienė, Gaškaitė, pp. 56/57.

[322] For details see www.freema.org/Research/Bankruptcy.phtml .

and other sides,[323] and another reform of the insolvency laws seems overdue. Major criticism levelled against the status quo includes:

- very low compliance with international standards;
- timeline of three months for the recognition of creditors' overdue debts is far too long;
- no recognition of a "balance sheet" test for insolvency;
- no provision on qualifications or requirements for insolvency administrators;[324]
- inefficiency in addressing reorganisation;
- no provision on cross-border insolvency proceedings;[325]
- ineffective operation of the laws in practice;[326]

[323] For instance, Strategy for Lithuania, Document of the European Bank for Reconstruction and Development of 23 March 2006 (in the following: EBRD Strategy), available at: http://www.ebrd.com/about/strategy/country/lith/strategy.pdf (visited: 30 August 2007), pp. 49-51; Juraj Strasser , Eliska Kutenicova, A commercial law perspective on the "graduation" of eight central European countries, EBRD Law in transition online, November 2006 (in the following: Strasser, Kutenicova).

[324] EBRD Strategy, p. 50; this criticism is only partly true as the law provides for the necessity of constant improvement of the professional qualifications of the administrator (Art. 11 (11) EBL) and the administrators are licensed and, at least in theory, supervised by Department for Enterprise Bankruptcy Management under the Ministry of Economy. The Departments website is available at http://www.bankrotodep.lt/ (visited: 30 August 2007).

[325] EBRD Strategy, p. 50. Strasser, Kutenicova, p. 3. In November 2007, the Lithuanian Parliament is expected to vote on a draft bill prepared by the Government and aiming at harmonising the Lithuanian insolvency laws with the European insolvency norms.

[326] EBRD Strategy, p. 50; The World Bank, Report on the Observance of standards and codes, ROSC, February 2002, (in the following: ROSC) available at www.worldbank.org/ifa/icr_ltu.pdf (visited: 31 August 2007), p. 14-15.

- no specialised judges or even courts deal with insolvency cases, and, it is even possible that different judges deal with different aspects of the same bankruptcy case;[327]
- abuse of the LRE by debtors for gaining time and protection against the institution of bankruptcy proceedings.[328]

Another issue which is raised is whether, in future, also bankruptcy proceedings against natural persons should be possible, as, for instance, in Germany (§§ 304 et seq. German Insolvency Code (InsO).[329]

2. Commencement of Insolvency Proceedings

a) Principles of Procedure and Legal Protection

Two major principles of the current insolvency laws in Lithuania can be discerned: One principle relates to the differentiation between restructuring procedures from bankruptcy procedures.[330] While restructuring procedures aim at furthering the rehabilitation of enterprises in temporary financial distress, the bankruptcy procedures focus on satisfying

[327] It is interesting to notice that Art. 12 para. 5 of the Law on Courts (LC) provides for the – as yet unused - opportunity to establish courts of special jurisdiction regarding bankruptcy cases. Lietuvos Respublikos teismų įstatymas. Valstybės žinios 1994, no. 46-851. Available also in English at http://www.lrs.lt/ (visited: 30 August 2007). Note that the available English version is not always up to date.

[328] Interview of the author with Head of Special Assets of a major bank in Lithuania. This abuse is possible due to the priority of the restructuring procedure as long as bankruptcy proceedings have not been instituted, cf. Art. 8 and Art. 15 para. 8, 24 LRE.

[329] Cf. Reinhard Bork Einführung in das Insolvenzrecht, 4th ed., 2005 (Bork Insolvenzrecht), pp. 410-419.

[330] This principle is evidenced by the existence of two separate laws to cover restructuring procedures (LRE) and bankruptcy procedures (EBL).

creditors in a fast-tracked procedure which almost inevitably leads to the liquidation of the debtor.[331] The second principle relates to the "predominance of creditors' group interests" over interests of individual creditors. This principle is reflected in the numerous provisions of the EBL and the LRE in which the interests of individual creditors are overruled by the interests of the creditors as a group.[332] The insolvency procedures are governed by the EBL and the LRE. Subsidiarily, other laws apply as stipulated by Art. 1 para. 3 EBL, Art. 1 para. 5, 6 LRE and the provisions governing the scope of applicability of other statutes, e.g. Art. 1 CCP.

Due to the aim of fast-tracking bankruptcy proceedings, legal protection is limited in insolvency proceedings. However, the EBL provides for an appeal mechanism. A separate appeal against the decision of the court to institute bankruptcy proceedings or against the decision to appoint, temporarily substitute for or dismiss the administrator may be submitted and must be heard by the Court of Appeals of Lithuania within two weeks from the date of its lodging. Having quashed the decision whereby institution of bankruptcy proceedings is refused, the Court of Appeals of Lithuania may not make a decision to instituting bankruptcy proceedings. The decision of the Court of Appeals of Lithuania is final and not subject to appeal by cassation (cf. Art. 10 para. 8 EBL). According to Art. 10 para. 13 EBL, the lodging of an appeal against the decision to initiate or dismiss a petition on the initiation of bankruptcy proceedings, prevents the court's decision from becoming effective, provided that the court's decision was made in written proceedings.

According to Art. 13[1] para. 9 a separate appeal may also be filed against the court order to apply simplified bankruptcy process. Another right to a separate appeal is set forth in Art. 26 para. 5 EBL, according to which a separate appeal against the court order to allow or refuse to allow creditors' claims may be filed only by the administrator and

[331] Art. 28 et seq. EBL provides for the possibility of concluding a composition agreement with the creditors. Yet, this only means of rehabilitation of a debtor against which bankruptcy proceedings have been initiated, is practically irrelevant. See above part 1 b) and below part 4 b).

[332] For instance, Art. 10 para.7 no. 3, Art. 34, 35 EBL, and Art. 9 para.1 no. 1, Art. 14 LRE.

creditors, with respect to whom the orders have been issued. Other creditors may appeal against the orders only provided that the total amount of the financial claims allowed by the orders exceeds LTL 250 (ca. EUR 73) and the amount of the allowed financial claims of the creditor who is filing the appeal exceeds LTL 250.

These appeals are made to a single appellate court. The term for appealing against decisions of the court is only indirectly determined in Art. 10 para. 13 EBL for the decisions mentioned in this norm, as the norm stipulates that the decisions enters into effect unless appealed within ten days from the day of its making. With respect to other rights to appeal, the EBL is silent on the terms. Therefore, as a rule, the appeal must be lodged within seven days of the day when the decision of the court in oral proceedings was passed or when the decision of the court in written proceedings was served (cf. Art. 1, 335 CCP). The panel shall consist of three judges appointed from the 26 appellate court judges. Insofar there is a risk that while handling separate appeals different judges hand down decision relating affecting the same case. This increases the potential for inconsistent rulings in general as well as in the bankruptcy case at hand.[333] In addition, the appeal system has proved to be slow and inefficient. Art. 24 para. 5 EBL stipulates a different kind of appeal relating to resolutions of the creditors' meeting. Such resolutions may be appealed against to court within 14 days from the day when the creditor learnt or should have learnt of the adoption of resolution.[334]

The LRE scarcely mentions the right to appeal in two places. First, it only indirectly provides for the right to appeal by stating in Art. 7 para.5 LRE that the order to initiate or to refuse to initiate restructuring proceedings becomes effective within ten days from the day of adoption thereof provided it was not appealed against.[335] Second, after restructuring

[333] See also the criticism in ROSC, p. 7.

[334] It is worth noting that the administrator is also entitled to appeal to the court, cf Supreme Court of Lithuania, decision of 7 December 2005, civilinė byla no. 3K-3-650/2005.

[335] Although not expressly mentioned in the LRE, the appeal must be lodged to the Court of Appeal in Vilnius (Art. 21 Law on Courts (LC), Lietuvos Respublikos Teismų įstatymas, Valstybės žinios, 1994, no. 46-851, Valstybės žinios, 2002, no. 17-649. Art. 1 para.1, Art. 334 CCP.

proceedings have been initiated, Art. 19 para. 7 LRE entitles creditors to appeal to the court against the resolutions of the meeting/committee of creditors.

b) Scope and Applicability

The scope of applicability of the EBL is wider than that of the LRE. None of them, however, applies to natural persons. The EBL applies to all enterprises, public agencies, banks and credit unions (together referred to by the EBL as "enterprises") which were duly registered in Lithuania (Art. 1 para. 2 sentence 1 EBL). However, specific features of bankruptcy processes of banks[336], credit unions, insurance companies, agricultural enterprises, intermediaries of public trading in securities, and other enterprises and institutions, may be established by other laws which regulate the activities of these enterprises and public agencies (Art. 1 para. 2 sentence 2 EBL).[337] In contrast, the LRE only applies to enterprises duly registered in Lithuania (Art. 1 para. 3 LRE). The LRE expressly excludes banks,[338] the central and other credit unions, other credit institutions, insurance companies, management companies, open-ended investment companies and intermediaries of public trading in securities from its scope of application.

[336] Specific regulations can be found, e.g., in Art. 78–87 of the Law on Banks (LB), Lietuvos Respublikos bankų įstatymas. Valstybės žinios, 2004, no. 54-1832, available also in English at http://www.lrs.lt/ (visited: 31 August 2007). Note that the available English version is not always up to date.

[337] Specific regulations can be found in, e.g., Art. 125-143 of the Law on Insurance, Lietuvos Respublikos Draudimo įstatymas, Valstybės žinios, 2003, no. 94-4246. It is not available in English. Art. 50 of the Law of Credit unions, Lietuvos Respublikos kredito unijų įstatymas, Valstybės žinios, 1995, no. 26-578, available also in English at http://www.lrs.lt/ (visited: 31 August 2007). Note that the available English version is not always up to date.

[338] Here, regulations can be found in specific laws, e.g. Art. 78 et seq. LB or Art. 61-74 of the Law on Companies (LC), Lietuvos Respublikos akcinių bendrovių įstatymas, Valstybės žinios, 2000, no. 64-1914. The laws are also available at http://www.lrs.lt/ (visited: 31 August 2007). Note that the available English version is not always up to date.

The provision of the EBL and LRE are applicable only to the extent they do not contradict the Law on Financial Collateral Arrangements and the Law on Settlement Finality in Payment and Securities Settlement Systems (Art. 1 para. 4 EBL and Art. 1 para. 6 LRE).[339] On the other hand, both the EBL and the LRE limit the applicability of certain laws when conflicting with the provisions in the EBL or the LRE. In this regard, the provisions of the EBL overrule other laws regulating the activities of enterprises, the creditor's right to the satisfaction of claims, the creditor's right to take measures to recover debts, taxes and other mandatory payments and the administration thereof in the course of bankruptcy process (Art. 1 para. 3 EBL). During restructuring provisions regulating the activities of enterprise, waiver of creditor's claims or a part thereof, postponement of deadlines for the discharge of obligations and making of compulsory payments apply only to the extent the LRE does not provide otherwise (Art 5 LRE).

c) Grounds for Opening Insolvency Proceedings

aa) Bankruptcy Proceedings

The EBL allows the opening bankruptcy proceedings, pursuant to Art. 9 para. 5 in case of (i) delay of payment of wages for at least three months or (ii) public announcement or notification of creditors about inability to effect settlement and pursuant to Art. 2 para. 8 in case of (iii) public announcement or notification of creditors about lack of intent to discharge liabilities, and (iv) "insolvency". Already the definition of illiquidity in (i) to (iii), leave room for argumentation about when the threshold has been reached and the court must institute bankruptcy proceedings.[340] The existing jurisdiction has been inconsistent; yet, a

[339] Valstybės žinios, 2004, no. 61-2183 and Valstybės žinios, 2006., no. 61-2754. Both laws are available also in English at http://www.lrs.lt/ (visited: 11 September 2007). Note that the available English version is not always up to date.

[340] For instance, the law is not clear on whether proceedings must be instituted with all ensuing consequences if one employee of many has not received an amount of money equalling three months salary (without a delay of three full months' wages in a row) or if an employ has not received 20% of his monthly salary for

tendency can be discerned whereby courts tend to restrict the scope of applicability of the ground (i) by introducing an unwritten precondition according to which employees' petitions must not be made in bad faith.[341]

However, "insolvency" as defined in the LBE (iv), is even harder to pin down. The definition demands an element of illiquidity (failure to settle with creditor(s)) and an element of over-indebtness (liabilities amounting to more than 50% of the value of the assets of the debtor). The element of illiquidity entails similar room for argumentation as the insolvency ground (i). In particular, it is unclear whether the non-payment of only a small part of the original debt suffices to trigger the bankruptcy proceedings.[342] Contrary to the impression one might have at first reading, the element of over-indebtness does not allow for a simple balance-sheet test.[343] In other words, the court competent to decide a petition for bankruptcy must not merely compare the book-values of the debts and assets in the enterprises balance sheet in order to verify whether the threshold-ratio of 50% has been reached. Rather, the court is tasked to take into account all information which is available to it in order to appraise the concrete financial situation of the enterprise. In this regard, two recent rulings of the Lithuanian Appellate Court confirmed this position of the jurisprudence which already dates back to

a period of three months in a row. Further, it might be difficult to differentiate between a "lack of intent to discharge liabilities" from raising legitimate objections against the creditor's claim (e.g. due to defects of a good received).

341 Some decisions even go so far that petitions are rejected unless they are submitted / supported by all employees of the enterprise. Petitions of individual employees are rejected and the individual employees referred to the possibility of bringing an ordinary action before the courts, cf. Appellate Court, decision of 22 April 2003, civilinė byla nr. 2-154/2003.

342 In practice, the claims of creditors against the enterprise are often disputed by the enterprise. Recent court decisions indicate that a mere delay in paying a debt is not sufficient for opening bankruptcy proceedings. The bankruptcy courts demand proof that the creditor's claim is undisputed or adjudicated. Creditors with disputed claims are referred to the ordinary civil proceedings, cf. Appellate Court, decisions of 6 April 2006, civilinė byla nr. 2-196/2006, and 1 June 2006, civilinė byla nr. 2-322/2006.

343 Cf. EBRD Stragety, p. 50.

the interpretation of the EBL 1997.[344] The reasoning is mainly based on Art 9 para. 2 EBL allowing the court competent to decide on a petition for bankruptcy to "obligate [certain natural persons] to submit to the court all documents required for the investigation of the bankruptcy case and to appraise the property of the enterprise" as well as to summon before the court certain persons and demand that they give explanations relating to the institution of bankruptcy proceedings.[345]

bb) Restructuring Proceedings

Restructuring of an enterprise may only commence if all of the following conditions are met (Art. 3 LRE):

- the enterprise fails to settle with its creditor(s) for more than three months after the due date of the obligation;
- the enterprise has not discontinued its economic and commercial activities;
- no bankruptcy proceedings have been initiated against the enterprise and no extrajudicial bankruptcy process has commenced.

In addition, a proposal or petition to initiate restructuring proceedings must have been duly filed to the court by a person entitled to do so (Art. 4-7 EBL). These prerequisites are described in more detail in part 2 d) ii below.

d) Persons Entitled and Persons Obliged to File the Petition/Proposal for Insolvency Proceedings

aa) Bankruptcy Proceedings

Art. 5 to 8 EBL stipulate who has a right/duty to file a petition for the institution of bankruptcy proceedings. In addition, Art. 4 EBL defines the grounds for filing a petition, i.e. it enumerates the conditions which have to be met for a valid petition. According to Art. 5 EBL,

[344] Lietuvos Apeliacinis Teismas, judgements of 10 May 2007 (Civilinė byla no. 2-309/ 2007) and of 19 July 2007 (Civilinė byla no. 2-494).

[345] The court might even request an expert's opinion, e.g. on the true value of an asset, according to Art. 1 para. 1, 212 et seq. CCP.

creditor(s)[346], owner(s)[347] and the head of the enterprise administration[348] are entitled to file a petition for the institution of enterprise bankruptcy proceedings. Further, under the conditions laid down in Art. 7 para. 1 EBL, the liquidator of the enterprise in liquidation is obliged to file the petition for bankruptcy (Art. 5 para. 2 EBL). All petitions must be filed in writing according to the manner set forth in the CCP with the competent court and must be accompanied by documents proving the reasonableness of the petition (Art. 5 para. 3, 4 EBL). The persons specified in Art. 5 EBL may file a petition for bankruptcy if at least one of the conditions (grounds for filing a petition) stated in Art. 4 EBL is present:

1. the enterprise fails to meet due payment obligations (Art. 4 para.1 – 3 EBL);[349]
2. the enterprise has made a public announcement or notified the creditor / creditors in any other manner of its inability or lack of intent to discharge its liabilities (Art. 4 para. 4 EBL);
3. the enterprise has no assets or income from which debts could be recovered and therefore the bailiff has returned the writs of execution to the creditor (Art. 4 para. 5 EBL).

Creditors' petitions are subject to certain qualifications set forth in Art. 6 EBL unless the enterprise already announced publicly or vis-?-vis the creditor its inability or unwillingness to discharge its liabilities (cf. Art. 4 para. 4 EBL). As a rule, creditors may file a petition for bankruptcy

[346] "Creditors" of the enterprise are defined in Art. 3 EBL and comprise all "legal and natural persons who have the right under law to demand from the enterprise the discharge of liabilities and obligations ....".

[347] "Owner(s)" means, according to the definition in Art. 2 para. 9 EBL, the owner(s) of an individual/personal enterprise, member(s) of a general partnership, general member(s) or limited member(s) of a limited partnership, founder of a state-owned or municipal enterprise, shareholder(s) whose shares carry over 10% voting rights, holder(s) of member share and stakeholders in a public agency.

[348] Note that the term "head of the enterprise administration" has the same meaning as "enterprise manager". The law uses these terms interchangeably, which does not add to the clarity of the law.

[349] Art. 4 para. 1 EBL relates to employment-related debts; Art. 4 para. 3 EBL to compulsory contributions prescribed by law (e.g. taxes) and awarded sums; and Art. 4 para. 2 EBL to other payment obligations and liabilities (e.g. for goods received).

only after the expiry of a three-month period commencing with the date when the obligations of the enterprise become due (Art. 6 para. 1 EBL). Further, before filing the petition, the creditor must notify the enterprise in writing of the intention to file a petition for bankruptcy, identifying the unsettled liability, setting an period for the discharge of the liability of at least 30 days and warning the enterprise that a petition for bankruptcy will be filed if the liabilities remain unsettled after the expiry of the additional period (Art. 6 para. 2 EBL). The creditor can do without these prerequisites of waiting three months and setting an deadline of at least 30 days only if the condition specified in Art. 4 para. 5 EBL is present and the creditor files a petition for bankruptcy no later than one month after the writs of execution were returned (Art. 6 para. 3 EBL). Copies of the petition must be presented to the enterprise (Art. 6 para. 4) and must be accompanied by evidence testifying that the requirements of the preconditions have been duly met. Creditors may waive filed petitions before the court passes a decision to institute bankruptcy proceedings (Art. 6 para.5 EBL). The three- month period which creditors are obliged to wait before they are entitled to file a petition for bankruptcy runs counter to the legislator's aim of avoiding the late filing of petitions and - compared to international standards - this period seems much too long.

Liquidators of the enterprise are obliged to suspend all payments and to file for instituting bankruptcy proceedings within 15 days from the day of establishing that the enterprise will be unable to discharge all its liabilities. This obligation and the formalities to be observed by the liquidator are set forth in Art. 7 EBL. The enterprise's manager and owner(s) are also obliged to file for the institution of bankruptcy proceedings if "the enterprise is and/or will be unable to settle with the [creditor(s)], and the latter have not filed a petition for bankruptcy ... or if the condition referred to in Art. 4 para. 4 is present." This obligation is triggered, except where the condition of Art. 4 para. 4 EBL is present, if the enterprise experiences either in a state of illiquidity or in a state of imminent illiquidity, provided that the creditors remain inactive. It is rather problematic since the law neither defines the state of illiquidity nor the state of imminent illiquidity which appears to be a foreign element in the EBL. Further, creditors are not entitled to file for bankruptcy before their claim is three months overdue. Therefore it seems unreasonable to link an obligation of the manager / owner of the enter-

prise (filing for bankruptcy) to a conduct of the creditor(s) (not filing for bankruptcy) as long as the creditor(s) are not entitled to act because the three-month period stipulated by Art 6 para. 1 EBL has not elapsed. The obligation under Art. 8 para.1 EBL has little practical impact not only for the problems described above. Moreover, a failure to comply with the obligation in Art. 8 para.1 EBL does not carry, per se, noteworthy sanctions.

Provisions on the civil liability of persons obliged to file petitions for bankruptcy are scarce in the EBL.[350] One risk which the enterprise's owner(s) and managing director face under the EBL when breaching their obligation under Art. 8 para.1 EBL is indirect, limited to LTL 10,000, and flows from the court's right under Art. 10 para. 10 EBL to recommend to the creditor who lodged the petition for bankruptcy to pay an amount of up to LTL 10,000 in order to finance a simplified bankruptcy process, provided that the court made a sufficiently justified assumption that the enterprise's assets are insufficient to cover legal and administration costs of a regular bankruptcy procedure in court. The creditor who pays the aforementioned amount in order to finance the simplified bankruptcy process may then apply to the court for the award of the paid sum from the enterprise manager and/or the owner(s) "for failing to file a petition for bankruptcy after the enterprise became insolvent." (Art 10 para. 11 EBL).

bb) Restructuring Proceedings

Creditor(s) may file in writing a proposal for restructuring to the head of the enterprise administration, provided that the creditor's/creditors' claim(s) meet the conditions stipulated in Art. 3 LRE (see above part 2 c) ii.). A creditor may either recover the debt by bringing an action in court or file a petition for initiating the enterprise restructuring proceedings, if

[350] Art. 50 para. 6 of the Law on the Violation of Administrative Laws (Administracinių teisės pažeidimų kodeksas, Valstybės žinios 1985 no. 1-1) establishes the administrative liability of enterprise managers and administrators who, i.a., do not fulfill their obligation to file a petition for bankruptcy proceedings or to call in a creditors meeting. The law stipulates an administrative penalty of LTL 5,000 to 10,000 (ca. EUR 1,450 to 2,900) and for the case of repeated offence LTL 10,000 to 50,000 (ca. EUR 2,900 to 14,500).

the enterprise fails to satisfy the claim(s) of the creditor(s) within 30 days from filing the proposal for restructuring or does not undertake the actions outlined in Art. 4 para.2 et seq. (Art. 4 para.1 LRE).[351] These actions aim at convening a first meeting of creditors with a goal of receiving the necessary consents of the creditors to entitle the head of the enterprise administration to file a petition in the court on initiating the restructuring proceedings.[352] Both the head of the enterprise administration and the creditor(s) may file a petition on initiating restructuring proceedings in the court. As a rule, this petition presupposes that a first meeting of creditors was convened and duly voted in favour of restructuring procedures.[353] This implies that creditors may only file a petition if the waiting period of three months and 30 days resulting from Art. 3 para.1 and Art. 4 para.1 has passed (Art. 5 para.1, 4, Art. 23 para.1 LRE).

3. Institutional Framework

a) Court

Bankruptcy cases are to be filed in (Art.5 EBL) and handled (Art.10 EBL) by the civil section of one of currently five county courts (Apygardos teismai) which enjoy subject-matter jurisdiction over bankruptcy cases

[351] This leads to a 3 months (Art. 3 LRE) + 30 days (Art. 4 LRE) waiting period, i.e. a creditor must wait even longer to be allowed to initiate restructuring procedures than to initiate bankruptcy proceedings (period: 3 months, see above 2 d).

[352] In special circumstances, the written consents of creditors in lieu of a affirmative vote in the first creditors meeting may suffice (cf. Art. 4 para. 5 LRE).

[353] Cf. Art. 4 para. 2, 4, 5 LRE regarding the voting procedure and majority requirements. The LRE places an emphasis on principal creditors, defined in Art. 2 para. 9 LRE as "creditor holding the discharge of whose claims is secured by a pledge and/or mortgage, a guarantee and/or a surety, or a creditor the amount of whose claims represents at least 1/5 of the aggregate amount of claims of all creditors."

(Art. 27 CCP).[354] Proper venue follows the location where the registered office of the enterprise situated (Art. 5, 10 EBL). This determination of the proper venue is especially problematic in cases in which the (main) economic activity of the enterprise happens in location(s) other than where the registered office is situated. In such cases the competent court in the sense of Art. 5, 10 EBL might be too far away from the enterprises main activities and assets. Further, the EBL's provisions relating to the proper venue are rudimentary in that they do not provide for regulations for concentration of bankruptcy proceedings in cases in which several enterprises of a group/concern go bankrupt. According to the status quo, the venue for each of the enterprises' bankruptcy proceedings have to be determined separately, although the group/concern relationship to affiliated companies might militate for concentrating the respective proceedings at one court.

In court, bankruptcy proceedings are investigated in contentious proceedings as prescribed by the CCP unless the EBL does not stipulate exceptions. This means that the case is usually handled by single judges in written proceedings, unless a motion for oral proceedings has been filed or the judge considers it necessary to proceed in oral proceedings (Art. 62, Art. 227-228 CCP, Art. 26 para. 4 EBL). Judges may be repudiated subject to the conditions in Art. 64 et seq. CCP. Petitions for restructuring cases must also be filed to the county court (Apygardos teismas) of the locality where the enterprise's registered office is located (Art. 5 para. 2 LRE).[355] Unlike the EBL (Art. 10 para. 1, 2), the LRE does not contain a specific provision stating which court is responsible for instituting and handling bankruptcy cases. From the context and Art. 4 CCP it is clear, however, that the county court in the sense of Art. 5 para. 2 LRE is called upon to perform these tasks.

[354] ROSC, p. 6. County courts are located in Vilnius, Kaunas, Klaipėda, Šiauliai, Panevėžys.

[355] The official English translation of the RLE wrongly postulates the subject-matter jurisdiction of the district courts thus creating the false impression that the subject-matter jurisdiction in bankruptcy cases varies from the one in restructuring cases. However, in the prevailing Lithuanian version, subject-matter jurisdiction for restructuring cases is vested in county courts (Apygardos teismai).

Currently, judges handling bankruptcy and restructuring enjoy "little training in commercial matters, or in the specialised areas on bankruptcy and restructuring."[356] This lack of specialisation causes the inefficient handling of bankruptcy and restructuring cases by the courts is aggravated by the fact that judges are often poorly equipped and overloaded.[357]

b) Bankruptcy Administrator and Restructuring Administrator

Upon instituting bankruptcy proceedings, the court appoints the administrator of the enterprise (Art. 10 para. 4 sentence 1 EBL) who, i.a., takes over from the managing bodies the assets of the enterprise, administers (Art. 11 para. 3 EBL) and realizes them pursuant to Art. 30 et seq. EBL.[358] If restructuring proceedings are instituted, the court appoints an enterprise administrator (Art. 17 para. 5 sentence1 LRE) who performs the functions outlined in Art. 17 para. 5 LRE, mainly as a coordinator and supervisor. In particular, the administrator is responsible for supervising or organizing the formulation of the enterprise restructuring plan (Art. 17 para. 5 no. 5 LRE). Administrators may be removed from office by the court (Art. 11 para. 8 EBL, Art. 17 para. 7 LRE).

The remuneration of the administrators is fixed in a contract of agency which must be concluded with the administrator. In the case of bankruptcy proceedings, the creditor's meeting authorizes its chairman to conclude the contract with the administrator on behalf of the enterprise (Art. 11 para. 5, Art. 23 para. 9 no. 1 EBL). The amount of remuneration and the procedure of payment is fixed by the first meeting of the creditors. The law suggests that the sum of remuneration depends on whether or not the enterprise in bankruptcy continues its business, the type and amount of the enterprise assets being sold as well as the complexity and number of proceedings instituted and civil actions brought against the enterprise. Payment of remuneration may be effected in a lump sum after the completion of the bankruptcy process or by instal-

[356] ROSC, p. 6.

[357] ROSC, p. 6. EBRD Strategy, pp. 50 et seq.

[358] Details will be outlined below in part 4.

ments in the course of the proceedings (Art. 36 para. 4, 5 EBL). The LRE is scarcer in providing guidelines. The first meeting of creditors is responsible for "[nominating] the candidate of the administrator, the terms and conditions of the contract of agency (the remuneration, duration of the contract ..., responsibility, etc.) [and determining] the amount of remuneration to be paid ...." (Art. 20 para. 2 no. 3 LRE) However, the LRE lacks guidance on the factors which should influence the remuneration of the administrator. Much criticism has been levelled against the regulations on remunerating bankruptcy and restructuring administrators. Currently, there are no Government guidelines in place with respect to the amount of remuneration and the procedure of payment. In practice, administrators conclude contracts of agency entitling the administrators to monthly remuneration payments, thus providing no incentive to accelerate or even end the insolvency proceedings. Several creditors have lodged complaints and/or actions. However, no significant judgement restricting this practice has been passed by courts.

Under the EBL and the LRE administrators may be a natural or legal person licensed to provide the services as a bankruptcy and/or restructuring administrator (Art. 11 para. 1 EBL, Art. 17 para. 1 sentence 3 LRE).[359] Apart from this, neither the EBL nor the LRE regulate the necessary qualifications for administrators. However, both contain a comparable provision stipulating who must not be appointed administrator. Generally, any person that might have an interest in the outcome of the proceedings is excluded (Art. 11 para. 4 EBL, Art. 17 para. 4 LRE). In 2001, the Minister of Economy issued resolution no 221 stipulating, i.a., the prerequisites for being entitled to receive the license required to provide services as a bankruptcy and/or restructuring administrator.[360] According to this resolution, in order to receive a licence for bankruptcy administration services a natural person must, i.a., have a good reputation, high education, good knowledge of the laws and at least three years' experience in an executive position or two years' experience as assistant to an bankruptcy administrator. In addition, such person must

[359] Administrators formed a National Association of Business Administrators (Nacionalinė Verslo Administratorių Asociacija) who maintains a website at www.nvaa.lt (visited: 2 September 2007). Cf. also ROS, p. 8.

[360] Resolution no. 221 of 5 July 2001 Valstybės žinios 2001 no. 59-2137.

pass an examination. With respect to legal persons, at least one third of the natural persons employed, however not less than two persons must fulfil the qualifications stipulated to become a bankruptcy administrator.[361] Responsible for qualifying and licensing is the "Commission for Certification of Administrators" under the Ministry of Economy which may also revoke issued licenses.[362] However, this regime faces criticism since the qualification standards and, in particular, the knowledge tested in the examination are regarded to be insufficient to guarantee the necessary quality and experience of the persons handling bankruptcy and restructuring cases.[363]

The Bankruptcy Management Department of the Ministry of Economy[364] at the Ministry of Economics is the primary regulatory and monitory institution for bankruptcy and restructuring administrators although it suffers from a lack of capacity too properly discharge its tasks.[365] Both the EBL and the LRE contain provisions on the liability of the administrators according to which a bankruptcy "administrator must compensate, according to the procedure established by laws, all losses inflicted through his fault" (Art. 11 para. 6 EBL) and the restructuring administrator "shall be held liable for the damage caused to the enterprise and/or creditors pursuant to the laws of [Lithuania]". It has been criticised that the framework for liability of especially restructuring administrators is not well developed in Lithuania and that they are not obliged to carry professional liability insurance.[366]

[361] The prerequisites for receiving a license for restructuring services differ slightly. With respect to bankruptcy administrators, Art. 11 para. 2 sentence 1 EBL demands that the head of the legal person must be entitled to provide bankruptcy administration services. Further details are stipulated in the 2006, Resolution No 4-376 of 10 October 2006.

[362] Resolution No. 221, ROSC, p. 7 et seq.

[363] ROSC, p. 7 et seq. EBRD Strategy, p. 50.

[364] Įmonių Bankroto Valdymo Departamentas, more information available under www.bankrotodep.lt (visited: 2 September 2007).

[365] ROSC, p. 7.

[366] ROSC, p. 8. Further, there seems to be no significant case law with respect to the administrators civil liability to compensate for damages.

c) Creditors' Meeting and Creditors' Committee

Under the EBL, the interests of the creditors as a group are represented by the creditor's meeting and, if established, the optional creditors' committee. The first creditors' meeting must be convened by the court or, on its direction, the administrator, not later than within 15 days after the effective date of the court order to allow the claims of the creditors (Art. 22 para. 1, 2 EBL).[367] Subsequent meetings may be convened by the court, the administrator, the chairman of the creditor's meeting and a creditor / creditors whose aggregate value of claims accounts for at least 10% of the sum total of all creditors' claims allowed by the court (Art. 22 para. 3 EBL). Each creditor is entitled to attend creditors' meetings and to vote in these meetings (Art. 21 para. 3 EBL) and only creditors have the right to vote, although other persons may be entitled to attend creditors' meetings (Art. 22 para. 6 EBL). The creditors' meeting enjoys ample rights, most of which are stipulated by Art. 23 EBL.[368] According to this, the creditors' meeting is, i.a., entitled to

- to decide on the formation and composition of the creditors' committee, and to delegate to the committee all or parts of the rights of the creditors' meeting;
- to request reports from the administrator on his activities, to approve said reports and to investigate creditors' complaints against the administrator;
- to change and approve the estimate of administration costs and to change the priority and procedure of covering the expenses as well as to fix the remuneration of the administrator;

[367] Upon making a decision to institute bankruptcy proceedings, the court must set a time limit of 30 to 45 days from the effective date of the court decision within which the creditors shall have a right to file their claims which arose prior to the day of institution of bankruptcy proceedings (Art. 10 para. 4, 5 EBL). The procedure of allowing creditors' claims by the court is set forth in Art. 26 EBL.

[368] Other rights are e.g. contained in the provisions on the liquidation procedure, e.g. Art. 33 para. 1, 2 EBL according to which the creditors decide on the sale of certain assets.

- to decide on the continuity, restriction or termination of economic-commercial activities of the enterprise and to submit motions to the court in this regard;
- to fix the numbers of employees to be employed during the bankruptcy process;
- to establish the manner whereby creditors, owner(s) etc receive from the administrator information about the course of the proceedings;
- to decide on compositions with creditors;
- to propose to the court the application of liquidations procedures.

Resolutions of the creditors' meeting are binding on all the creditors (Art. 24 para. 4 EBL). They may be appealed against to the court pursuant to Art. 24 para. 5 EBL. Resolutions are adopted by open ballot and require the affirmative vote by creditors whose amount of claims allowed by the court accounts for over one half of the total amount of allowed claims of all creditors (Art. 24 para. 1 EBL).[369] The law provides for the possibility of a repeat meeting within 15 days in which the creditors' may vote, as a rule, only on the same subject-matter as before and in which a resolution only needs the majority vote (in terms of value of claims) of the attending creditors (Art. 24 para. 2, 3 EBL).

Art. 25 EBL regulates the creditors' committee. This optional body may be elected by the first or by subsequent meetings of the creditors. Its task is to monitor the course of bankruptcy and the administrator's activities, to protect the creditors' interests in the periods between the creditors' meetings and to perform the tasks delegated to it by the creditors' meeting. The creditors' committee is composed of at least five members. If employment related claims exist, one member must be authorized to defend such claims. Its resolutions presuppose a quorum of at least half of its members. One member has one vote. Resolutions are adopted by simple majority vote during which, in case of a tie, the chairman's vote is decisive.

The LRE also provides for a representation of the creditors' interests by the creditors' meeting and the optional creditors' committee (Art. 20, 22 LRE). The functions and rights of these bodies are comparable to those in the realm of bankruptcy proceedings (see above and Art. 20

[369] Creditors' claims and the sum thereof must be reduced by the amount of sums paid out prior to the respective meeting.

LRE). However, the provisions in the LRE take account of the increased autonomy of creditors in restructuring proceedings in relation to the court. They also pay attention to the fact that the enterprise's management is not replaced by an administrator as is the case in bankruptcy proceedings. The increased autonomy is reflected, for instance, in the right to decide on whether an administrator will be appointed for the period of the implementation of the restructuring plan, and to nominate the candidate (Art. 20 para. 3 no. 4 LRE). The involvement of the enterprises management during restructuring is evidenced, e.g., by Art. 16 para. 1 LRE according to which the managing bodies of the enterprise continue to direct the activities of the enterprise although the creditors' committee enjoys the right to apply to the court to suspend powers of the members of the enterprise's managing bodies and to remove members of these bodies, including the head of the enterprise's administration, from office (Art. 20 para. 3 no. 8 LRE). In contrast to the provisions on creditors' committee's in bankruptcy proceedings, the LRE does not establish rights of persons other than creditors to attend creditors' meetings.[370]

The first meeting of creditors on initiating the enterprise restructuring proceedings is convened by the head of the enterprise administration (Art. 23 para. 1 LRE). Subsequent meetings may be convened by the enterprise administrator, the chairman of the creditor's meeting or the court. The head of the enterprise administration and the creditors whose claims amount to at least 10% of the aggregate amount of all claims are entitled to request "that the chairman of the creditors' committee convene a creditors' meeting (Art. 23 para. 2 LRE). From the context and aim of this provision, it must be assumed that the legislator wanted to refer to the chairman of the creditors' meeting and not – as is written – to the chairman of the creditor's committee.[371]

Voting by the creditors' meeting presupposes a quorum of at least 50% of the aggregate amount of the claims of all creditors (Art. 21 para. 1 LRE). The creditors' meeting adopts its resolutions either by voting

[370] No court seems to have adjudicated the question of rights of participation in creditors' meetings of persons other than creditors.

[371] No court seems to have adjudicated on this issue.

collectively or by groups.[372] When voting collectively, a resolution requires for adoption at least 50% of the aggregate amount of claims confirmed by the court, unless the LRE provides otherwise. If the meeting decides to vote by groups, "the resolution shall be considered adopted in each group, if the creditors the amount of whose claims made up at least 2/3 of the aggregate amount of claims by the creditors in this group voted in favour of it, unless [the LRE] provides otherwise." (Art. 21 para. 2 sentence 3 LRE) The total amount of votes casted in all groups must not be less than 2/3 of the aggregate amount of claims of all creditors (Art. 21 para. 2 LRE). The wording of the LRE with respect to voting by groups is not clear on whether a resolution requires the consent of all groups or only a simple majority of group consents (in addition to the requirements outlined above). Art. 21 para. 2 sentence 2 LRE and Art. 15 para. 5 LRE (argumentum e contrario),[373] however, indicate that, as a rule, a majority of consenting groups suffices to adopt a resolution. The provisions on repeat meetings resemble those for voting in bankruptcy procedures (see above). Exceptions exist for voting on the approval of the restructuring plan and on termination or closure of restructuring (Art. 21 para. 6 LRE).

The creditors' committee's rights, composition, voting etc are regulated in Art. 22 LRE. As a rule, the provisions are comparable to those of the creditors' committee in bankruptcy proceedings (see above). One major difference is that the Art. 22 para. 2 LRE stipulates in more detail than Art. 25 LBE, whose interests must be represented in the committee, who may become member of the committee and who may attend its meetings.[374]

[372] For voting by groups, the following five groups of creditors must be formed (i) secured creditors (ii) employees with employment related claims as well as claims to pay for agricultural produce purchased for processing (iii) administrators of compulsory payments (iv) unsecured creditors of long-term loans with unexpired repayment terms (v) other creditors (Art. 21 para. 3 LRE.

[373] Art. 15 para. 5 LRE relates to voting in groups on the restructuring plan. In this case, the LRE requires that all groups enumerated in Art. 3 para. 3 no. 1-5 LRE consent.

[374] In particular, one member must be a person authorized to defend employment related claims, a second must be a person representing the interests of secured claims.

4. Insolvency Proceedings

a) The Different Kinds of Proceedings

Currently, there are five different kinds of insolvency proceedings under the LBE and LRE: (i) bankruptcy proceedings, (ii) extrajudicial bankruptcy process, (iii) simplified bankruptcy process, (iv) composition[375] with creditors and (v) restructuring proceedings (also providing for simplified restructuring proceedings). These proceedings can be structured according to their legal source, the aim of the proceeding, or whether a court is involved in the proceedings or not. The insolvency proceedings (i) to (iv) are regulated by the LBE, the proceeding (v) by the LRE. The proceedings (i) to (iii) aim at realizing the enterprise's assets through liquidation whereas proceedings (iv) and (v) focus on the enterprise's rehabilitation. Only (ii) is a true out-of-court settlement of the enterprise and its creditors whereas the others require the involvement of a court.

The relationship between bankruptcy and restructuring proceedings is determined by the EBL and LRE. These reflect the aim of the legislator to further the rehabilitation of enterprises. Where a petition for restructuring is received during the investigation of the petition for bankruptcy and the court decision to institute bankruptcy proceedings has not yet been issued, the investigation of the petition for bankruptcy must be postponed pending the court order to initiate restructuring proceedings or to refuse to grant the petition for restructuring (Art. 9 para. 4 EBL, Art. 8 LRE). The vast majority of insolvency proceedings is handled in court and ends with the liquidation of the enterprise. Against this background, the following explanations focus on the standard bankruptcy proceedings in court. The other proceedings are described in less detail.

The aim of the period following the petition for bankruptcy proceedings is to evaluate whether there exists a ground for instituting bankruptcy proceedings and whether the enterprise possesses sufficient assets

[375] A composition with creditors is not a separate proceeding in the narrow sense of the word. Yet, it will be dealt with separately below in part 4 e), as the relevant norms stipulate a specific procedure to terminate bankruptcies.

to cover legal and administration costs (Art. 9 para. 5 EBL and Art. 10 para. 10 EBL). The competent court must decide within one month after receipt of the petition whether to institute bankruptcy proceedings or to refuse the petition. The court may extend this period for a maximum of one month, provided there is a valid reason (Art. 9 para. 4 EBL). In order to enable the court to make its decision, Art. 9 para. 2 EBL grants the court ample powers, e.g.,

- to obligate enterprise owner(s), members of the enterprise's management bodies, chief accountant(s) and the liquidator to submit all necessary documents;
- to summon before the court these persons (except the liquidator) and other executive officers whose employment contracts had been terminated in the twelve months prior to the day of filing of the petition, and to demand that they give written explanations;
- to summon before the court creditors of the enterprise;
- to request the manager or owner(s) to provide the court with data on the economic and financial position of the enterprise.

Further, on its own initiative or that of an interested person, the court may apply provisional measures according to the procedure of the CCP until the entry into force of the decision to institute or refuse bankruptcy proceedings (Art. 9 para. 2 no. 5 EBL). It may also determine other circumstances which are of importance for the investigation of the case (Art. 9 para. 2 no. 2, 6 EBL).[376] After a petition has been filed with the court, creditors who have duly obtained writs of execution against the enterprise may attach assets and funds of the enterprise, however, the sale and levying of assets and funds is staid (Art. 9 para. 3 EBL). The court must refuse instituting bankruptcy proceedings if (i) before the court's decision the enterprise satisfies the claims of the creditor(s), who filed a petition, or (ii) restructuring proceedings have been instituted, or (iii) the court makes a sufficiently justified assumption that the enterprise

[376] The court is, e.g., entitled to request an independent expert's opinion on the question of insolvency according to Art. 9 para. 2 no. 6 and Art. 212 et seq. CCP.

possesses insufficient assets to cover legal and administration costs[377] (Art. 10 para 3 no. 3 EBL).

b) Extrajudicial Bankruptcy Process

Among the five different kind of insolvency proceedings, the extrajudicial bankruptcy process is the only one which does not presuppose the court's involvement. The extrajudicial bankruptcy process is governed by Art. 12 and 13 EBL. It may only be applied if neither actions have been brought in court in which claims have been asserted against the enterprise nor executions levied on the enterprise under writs of execution issued by courts or other institutions (Art. 12 para. 1 EBL). The extrajudicial bankruptcy process may be carried out if "the enterprise is unable and will not be able to settle with [its creditor(s)]" (Art. 12 para. 2 EBL, emphasis added).[378] In order to start the process, the manager of the enterprise or its owner(s) must notify every creditor in writing of the motion to implement extrajudicial bankruptcy procedures, at the same time indicating the date and place of the creditor's meeting. The creditors' meeting must be convened within 20 days from the day when the aforementioned motion was sent to the creditors. The decision to carry out extrajudicial bankruptcy procedures requires a affirmative vote by the creditors whose claims in terms of value account for a at least 4/5 of the amount of the enterprise's liabilities on the day of adoption of the resolution, including those which have not yet matured (Art. 12 para. 4 EBL). If the motion is rejected, the persons listed in Art. 5 para. 1 EBL[379] are entitled to file to court a petition for bankruptcy without having to adhere to the time limits set forth in Art. 6 para. 1 EBL and the prerequi-

[377] Except for the cases in which a creditor makes a payment to the court to institute the simplified bankruptcy process (Art. 10 para. 3 no. 3, para. 10 EBL) or the claims of the filing creditor are employment related in which case, too, the simplified bankruptcy process may be instituted (Art. 10 para. 3 no. 3, para. 12 EBL).

[378] Note the different wording as compared to Art. 8 para. 1 EBL (emphasis added): "... enterprise is and/or will be unable to settle ...."

[379] See above part 2 d).

site of (lasting) illiquidity described in the above paragraph, provided that the petition to court is filed within 30 days after the creditors' meeting (Art. 12 para. 5 EBL). During extrajudicial bankruptcy procedures, the competences of the bankruptcy court are vested in the creditors' meeting which, i.a., appoints the bankruptcy administrator (Art. 13 EBL).

c) Effect of the Opening of Bankruptcy Proceedings

The court's decision in written proceedings to institute bankruptcy proceedings comes into effect within ten days after its making, unless an appeal is lodged against it (Art. 10 para.13 EBL). In effect, the decision has a significant bearing on the enterprise's management, its representation before and outside court, the recovery of claims, and other areas. In particular, the decision has the following direct consequences:

- The enterprise's managing bodies lose their powers (Art. 10 para.7 no. 2 EBL). The right to manage, use and dispose of the assets/funds of the enterprise in bankruptcy is vested in the bankruptcy administrator (Art. 14 para. 1 EBL). Contracts entered into in violation of this provision are null and void (Art. 14 para. 2 EBL).
- The administrator is the only person entitled to represent the enterprise outside and before the courts (Art. 14, 15 para. 3, Art. 11 para. 3 no. 6-9, 11 EBL).[380]
- All civil and criminal proceedings related to the bankruptcy case and the enterprise in bankruptcy are concentrated at the bankruptcy court (Art. 14 para. 3, Art. 15 para. 2, 3, Art. 18).
- Creditors may only recover claims against the enterprise in accordance with procedure laid down by the EBL. In particular, bailiffs must deliver to the bankruptcy court writs of attachment and writs of execution obtained by creditors prior to the institution of the proceedings (Art. 18 EBL). Also, the discharge of liabilities not met prior to the institution of bankruptcy proceedings including the recovery

[380] However, the administrator may issue further authorizations (cf. Art. 11 para. 3 no. 9, Art. 15 para. 3 EBL).

of debts from the enterprise through court or without suit is prohibited (Art. 10 para. 7 no. 3 EBL).[381]

- All debts of the enterprise in bankruptcy shall be considered overdue (Art. 16 EBL).

In addition, the decision has important indirect implications. Especially,

- As a rule, unexpired contracts entered into by the enterprise are deemed to have expired 30 days after the decision to institute bankruptcy proceedings, and claims arising due to this are to be met according to the sequence and procedure set forth in Art. 35 EBL (Art. 10 para. 7 no. 4, Art. 16 EBL). The law stipulates exceptions for employment contracts (see below) and "contracts from which claims of the enterprise in bankruptcy arise." (Art. 10 para. 7 no. 4 EBL)[382] Subject to the conditions in the EBL, the administrator is entitled to terminate unexpired contracts and enter into new agreements necessary for the enterprise to continue its economic-commercial activities provided that the enterprise continues its economic-commercial activities. If the administrator decides to enter into contracts for the lease of the enterprise assets, the day of expiry of the contract of lease must be the day of sale, transfer or return of the assets (Art. 11 para. 3 no. 7, 11, 13, Art. 17 para. 2 EBL).
- The administrator must within three working days from the effective date of the decision to institute bankruptcy proceedings give written notice to the employees on the termination of the employment contracts and dismiss the employees within 15 working days from such notification (Art. 11 para. 3 no. 11, Art. 19 EBL). Employees are entitled to severance pay in the amount of two average monthly wages (Art. 19 para. 2 EBL). Settlement with the dismissed employees follows the procedure set forth in Art. 35 EBL, i.e. is subject to

[381] Prohibitions to discharge financial liabilities and to recover debts are not applied in the cases set out by the Law on Settlement Finality in Payment and Securities Settlement Systems and the Law on Financial Collateral Arrangements (Art. 10 para. 7 no. 3 EBL).

[382] This wording in Art.10 para. 7 no. 4 EBL refers to reciprocal contracts with respect to which the administrator may choose whether to continue or to end the contract.

the sequence and procedure of satisfying claims of unsecured creditors (Art. 19 para. 3 EBL).[383] Employment contracts with members of the enterprise board and the manager must be terminated upon a 15-day written advance notice. These persons are not entitled to severance pay or compensation, except for monetary compensation for unused holidays (Art. 10 para. 7 no. 3 EBL). Claims relating to employment relationship and mentioned in Art. 35 para. 2 EBL may be met from the resources of the Guarantee Fund (Art. 35 para. 7 EBL).

d) Rescission and Invalidity of Pre-Petition Transactions

The bankruptcy administrator is obliged to examine the contracts of the enterprise entered into within an at least 36 months period before the institution of bankruptcy proceedings and bring actions for the invalidation of the contracts which are contrary to the objectives of the enterprise activities and/or which could have led to the disability of the enterprise to settle with its creditors (Art. 11 (para. 3 no. 8 EBL). The creditors may apply to the court for the establishment of a fraudulent bankruptcy (Art. 21 para. 1 no. 2 EBL) which is defined as "deliberate bringing of the enterprise to bankruptcy" (Art. 2 para. 12 EBL). If the court establishes a fraudulent bankruptcy, the administrator is obliged to review all contracts of the enterprise concluded within the five-year period prior to the institution of bankruptcy proceedings and bring an action before the court for the invalidation of the contracts which are contrary to the interests of the enterprise and/or which could have contributed to its loss of ability to settle with the creditors (Art. 20 EBL). In summary, apart from being concluded within the respective period of 36 months or five years, in order to be voidable, the contract (i) must be contrary to the objectives of the enterprise and/or (ii) must have increased the chance that the enterprise is not able to settle with its creditors.

[383] During the period from 1993 until 2000, according to ROSC p. 5 employees recovered an average percentage of repayment of claims of 34% (not adjusted to present value and inflation over the course of the proceeding).

e) Status of Secured Creditors

Secured creditors enjoy preferential treatment under the EBL with respect to the satisfaction of their claims.[384] The creditor's claims secured by pledge and/or mortgage must be paid first of all from the proceeds obtained from the sale of the pledged assets of the enterprise or by transferring the pledged assets (Art. 34 EBL). If the pledged assets are sold at a price exceeding the amount secured by the pledge and/or mortgage, the excess balance is to be allotted for meeting the claims of other creditors pursuant to the sequence and proceedings set out in Art. 35 EBL. However, proceeds from the sale of pledged assets are not excluded from being included in the funds which serve to cover the administration costs (Art. 36 para. 1 EBL, see below for more details). Apart from the above privilege, no other privileges are granted under the EBL, e.g. no additional rights in the creditors meeting.

f) Realisation of Debtor's Property (Liquidation of Bankrupt Enterprise)

The debtor's property is realized under the EBL by liquidating the bankrupt enterprise. The court must declare the enterprise bankrupt and issue the liquidation order if an order to conclude the composition with the creditors is not issued within three months from the effective date of the order to allow the creditors claims[385] and the court has not granted an extension of the deadline. Such extension may only be granted if so requested by the creditor's meeting (Art. 30 para. 3, Art. 23 para. 12 EBL). From the effective date of the court order, the enterprise acquires the status of enterprise in liquidation. The functions of the liquidator are

[384] A preferential treatment exists also under the LRE, see below part 4 i).

[385] The procedure for allowing creditors' claims is set forth in Art. 26 EBL according to which claims are allowed by the court in, as a rule, written proceedings. A separate appeal may be lodged against the decision to allow or refuse to allow a claim, provided that the preconditions in Art. 26 para. 5 EBL are met (see above part 2 a)). Creditors are entitled to a general or limited waiver of their claims and may also assign their claim to other creditors or persons (Art. 26 para. 2, 3 EBL).

performed by the administrator in accordance with the EBL (Art. 30 para. 4 EBL). His rights and duties are set forth in Art. 31 EBL and include the disposal of the enterprise assets and resources, the organisation of the sale of the assets and the satisfaction of the creditors' claims allowed.

The enterprise assets are appraised and sold in the manner specified in the EBL. Immovable property must be sold by auction according to the procedure established by the Government.[386] The creditors must decide the procedure of sale of other assets, except pledged assets. Unsold assets may be transferred to the creditors (Art. 33 para. 1 EBL). Shares and other securities of companies held by the enterprise must be sold to the highest bidder according to the procedure laid down by legal acts regulating trading in securities,[387] except for shares of private companies, which must be sold in the manner established by the creditor's meeting (Art. 32 para. 2 EBL).[388] Pledged assets must be sold by auction according to the procedure established by the Government. If the administrator transfers the unsold pledged assets to the pledgee / mortgage creditor, these persons must within 30 days from the day of transfer of the assets defray the expenses of asset administration.

The creditors whose claims have not been satisfied due to the insufficiency of funds shall decide on the use of the unsold assets. If not all property of the bankrupt enterprise has been sold or transferred to the creditors and not all claims of the creditors have been satisfied within 24 months from the effective date of the court order to declare the enterprise bankrupt, the liquidation procedure shall be considered completed (Art. 33 para. 4 EBL). The EBL establishes the following sequence of satisfaction of creditors' claims (Art. 34, 35, 36 EBL):

1) Administration costs are to be paid with all types of funds (proceeds from the sale of assets, including pledged assets, debts repaid to the enterprise, earnings from economic activities, rent for leased assets and other funds received in the course of bankruptcy, see Art. 36 EBL);

386 Valstybės žinios, 2001, No. 58-2090.

387 Law on Markets in Financial Instruments, Lietuvos Respublikos Finansinių priemonių rinkų įstatymas, Valstybės žinios, 2007, No. 17-627.

388 Note that shareholders of a private company the shares of which are offered for sale enjoy a right of pre-emption (Art. 33 para. 2 EBL and Art. 47 LC.

2) Creditor's claims secured by pledge and / or mortgage (only in respect of the proceeds from the sale of mortgaged / pledged assets, see Art. 34 EBL) ;
3) Claims arising from employment relationships, claims for the compensation of damage caused by grievous bodily harm or some other injury, an occupational disease or death due to an accident at work; claims for payment for agricultural produce purchased for processing (see Art. 35 para. 2 EBL);
4) Claims for payment of taxes and other payments into the budget, for compulsory state social insurance contributions and compulsory health insurance contributions; claims relating to loans obtained on behalf of or guaranteed by the State (see Art. 35 para. 3 EBL);
5) Claims other than those specified above (see Art. 35 para. 4 EBL).

The Creditors' claims above no 3) to 5) are satisfied in two stages. In the first stage the creditors' claims are satisfied in the sequence outlined in Art. 35 EBL excluding interest and penalties. In the second stage, the remaining part of the creditors' claims (interest, penalties) is paid in the same sequence. Claims of creditors of each successive sequence may only be met after full payment of the claims of the creditors of the preceding sequence (Art. 35 para. 1 EBL). If the assets are insufficient to satisfy all claims of one sequence in full, the said claims are paid in proportion to the amount due to each creditor (Art. 35 para. 6 EBL). As indicated above in part 4 b) ii, employees' claims may be met from the resources of the Guarantee Fund. Claims of persons for payment of agricultural produce purchased for processing by the enterprise may be met according to the procedure established by the Government.[389] Payments by the aforementioned third parties are to be subtracted from the allowed claims of the creditors (Art. 35 para. 7 EBL).

g) Simplified Bankruptcy Process in Court

The option of a simplified bankruptcy process was amended to the EBL in 2002 to address the significant number of cases in which bankruptcy proceedings could not be instituted due to fact that the enterprise's

[389] Valstybės žinios, 2007, No. 44-1690.

assets were insufficient for covering the legal and administration expenses.[390] Against this background, the simplified bankruptcy process may only be applied in the cases provided for in Art. 10 para. 10, 12 EBL and/or when the administrator establishes during the hearing of the enterprise bankruptcy case that the enterprise possesses not sufficient assets to cover legal and administration costs (Art. 13^1 para. 1 EBL). The decision to institute simplified bankruptcy procedures may be appealed against (Art. 13^1 para. 9 EBL). While the extrajudicial bankruptcy process is characterized by the absence of an involvement of the court as well as a dominating position of the creditors' meeting, the provisions of the simplified bankruptcy process vest more rights in the court in order to facilitate and accelerate the procedures (Art. 13^1 EBL). In fact, the meeting of the creditors is not convened during simplified bankruptcy proceedings (Art. 13^1 para. 10 EBL) During the process which may not last longer than one year from the effective date of the order to apply the simplified bankruptcy process, the procedure of liquidation must be applied (Art. 13^1 (1) EBL).

h) Composition with the Creditors

Composition with creditors is legally defined in Art. 2 para. 11 EBL as an "agreement between the creditors and the enterprise to continue the activities of the enterprise where the latter assumes certain liabilities, whereas the creditors agree to defer the satisfaction of financial claims or to reduce the amount thereof or to waive their claims." A composition with the creditors may be concluded at any stage of bankruptcy process until the court order to liquidate the enterprise by reason of bankruptcy becomes effective (Art. 28 para. 3 EBL), irrespective of the nature of the proceedings. In the case of extrajudicial bankruptcy process, the composition with the creditors is subject to notarial verification (Art. 29 para. 6 EBL). Creditors, the administrator and the enterprise owner(s) may file a motion to conclude a composition with the creditors (Art. 28 para. 1 EBL). The composition must specify the concessions made for the enterprise and the creditors' claims, the liabilities of the

[390] Valstybės žinios, 2002, no. 116-5193.

enterprise, the ways and schedule of satisfaction of claims and the liability of the enterprise in case of failure to carry out the composition agreement (Art. 29 para. 1). The composition must be signed by all creditors or their representatives and the administrator, after the latter has received the written consent of the enterprise owner(s) and the managing body which has the right to decide on liquidating or reorganizing the enterprise (Art. 28 para. 2 EBL).[391] Further, the composition requires the approval by the court. The court must refuse to approve the composition with creditors if actions provided for in the agreement contradict the laws or infringe somebody's rights and interests protected under law (Art. 29 para. 2, 3 EBL). The composition with the creditors comes into force on the effective date of the court order to approve the arrangement (Art. 29 para. 4, 5, Art. 27 EBL).

i) Restructuring under the LRE

Some major features of the LRE have been described above.[392] Therefore, this part will focus on remaining issues. Upon receiving a petition to initiate restructuring proceedings, the court must investigate whether the conditions precedent for opening restructuring proceedings exist (Art. 7 para. 1, 2 LRE). The court enjoys similar rights as in the case of bankruptcy procedures, i.e., it may obligate key persons to produce to the court additional documents, summon these persons to appear in the court and request written explanations (Art. 6 LRE). In certain cases the court must refuse to initiate the proceedings (Art. 7 para. 2 LRE): satisfaction of the claim of the creditor(s) who applied to the court; failure by the applying person to provide the necessary documents for proving the conditions precedent for restructuring proceedings; initiation of bank-

[391] The requirement that all parties involved in a bankruptcy proceedings must consent to the composition agreement renders this instrument impracticable. According to the official statistic of the Department of Enterprise Bankruptcy Management, available at http://www.bankrotodep.lt/?Lang=Change (visited: 11 September 2007) only 59 out of 4,910 bankruptcy proceedings instituted between 1993 and 1 July 2006 have been terminated or composition agreements with the creditors have been concluded.

[392] See above parts 1 to 3 with respect.

ruptcy proceedings against the enterprise. When ordering the initiation of restructuring proceedings the court must, at the same time, appoint the enterprise administrator for the period of developing the restructuring plan or any other period established by the meeting of creditors (Art. 7 para. 3, 20 para. 3 LRE). Further, the court must establish the time limit for submitting to the enterprise the claims of the creditors. This period of time must be between 30 and 45 calendar days (Art. 7 para. 5 no. 4 LRE). The decision to initiate restructuring proceedings has, i.a., the following effects (Art. 9 para. 1 LRE):[393]

- It is prohibited to discharge liabilities , to recover debts from the enterprise in a judicial or extrajudicial manner, to apply judgement mortgage, servitudes, usufruct, to offset claims, to pledge (with certain exception), sell or transfer in any other way the assets of the enterprise necessary for the continuation of its activities;
- Calculation of default interest and late penalties for all existing liabilities is stayed;
- Recovery under writs of execution and a set-off of the claims is suspended if they are not provided for in the restructuring plan;
- If it is necessary during restructuring to sell the pledged property, the property must be sold by the consent of the pledgee after the annulment of its pledge and/or mortgage, except for case when the buyer agrees to buy the pledged property;
- Creditors may make concessions with regard to the discharge of debts which accrued before the day when the court order to initiate proceedings became effective, relinquish the aggregate amount of the claims or a part thereof, and/or replace the pecuniary obligation by any other obligation; they also may give their consent that the enterprise settles liabilities from the assets of the enterprise and its shares.

During restructuring the enterprise must make all current payments unless it has entered into agreements with the creditors about the deferral of the payments or their replacement by any other obligation (Art. 10 LRE). Similar to bankruptcy proceedings, the administrator is called

[393] Art. 9 para. 2 LRE regulates the effects of the court order to discontinue restructuring proceedings.

upon to review the contracts entered into by the enterprise during the period of at least 12 months preceding initiation or restructuring proceedings and, subject to an affirmative resolution of the creditors' meeting/committee, bring actions in the court investigating the restructuring case for the invalidation of the contracts which are contrary to the objectives of the enterprise and/or which might have led to the inability of the enterprise to settle with creditors (Art. 17 para. 5 no. 4 LRE).[394] The LRE grants preferential treatment to secured creditors and to principal creditors. As in bankruptcy proceedings, secured creditors' claims are satisfied first of all (see below). Principal creditor "means a creditor the discharge of whose claims is secured by a pledge and/or mortgage, a guarantee and/or a surety, or a creditor the amount of whose claims represent at least 1/5 of the aggregate amount of claims of all creditors (Art. 2 para. 9 LRE). Such creditors play a major role while initiating the restructuring proceedings (e.g. Art. 4 para. 2, 4 LRE).

The key element for restructuring is the restructuring plan ("Plan"). The guidelines for the Plan must already be approved by the first creditors' meeting (Art. 20 para. 2 no. 5 LRE). The formulation of the Plan is supervised by the administrator who may also be charged by the creditors to organize its formulation (Art. 16 para. 2, Art. 17 para. 5 no. 5, Art. 20 para. 2 no. 3 LRE). After approval by the creditors, the Plan must be filed with the court for approval (Art. 17 para. 5 no. 7 LRE). During the period of drafting the Plan, the enterprise must not, without permission of the court (Art. 16 para. 3, 4 LRE):

- sell or transfer the enterprise or parts thereof, long-term assets or property rights, or transfer them without remuneration;
- grant securities for the discharge of obligations if no exception provided for in the law applies.

The Plan must be filed in the court within four months from the effective date of the court order to initiate proceedings. The court may extend this period for a maximum of one month. If this deadline is missed, the court must issue an order to discontinue the restructuring

[394] The wording of the law ("at least") leaves room for speculation if the administrator would also be entitled to bring actions for invalidation of contracts which were concluded longer than twelve months before initiating proceedings. There seems to be no case law on this question.

proceedings (Art. 15 para. 8, Art. 24 para. 1 no. 1 LRE). The Plan must, i.a., specify the following (Art. 13 LRE):

- aims and duration of restructuring;
- the enterprise business plan for the period of restructuring;
- assets necessary for economic and commercial activities and assets which will be sold;
- the arrangements for sale of assets and the purpose of the proceeds obtained;
- assets which are to be re-appraised or written off in the manner prescribed by the laws;
- agreements to be terminated, with the exception of employment contracts concluded prior to the day of commencement or restructuring proceedings;
- the amount, terms, conditions and guarantees of/for anticipated credits;
- future arrangements with creditors over reduced satisfaction of their claims;
- list of creditors with details on their claims;
- groups of creditors;
- claims against and claims of the enterprise which are subject to litigation;
- number of employees to be laid off;
- procedure of reporting about the implementation of the plan and of reporting by the administrator to the creditors' meeting/committee;
- restrictions on the head of administration and other managing bodies of the enterprise;
- estimate of administrative expense.

The Plan may be modified subject to the approval by the court. The Plan must also provide for the sequence of meeting creditors' claims as follows (Art. 14 LRE):

- claims of creditors subject to a pledge and/or mortgage (interest and default not included), which must be satisfied first of all from the proceeds of the sale of the pledged property;
- claims of employees relating to employment relations, claims for compensation for injury, occupational disease or death due to an accident at work; and persons' claims for payment for agricultural produce purchased for processing;

- claims for compulsory payments (e.g. tax, social security contribution) and loans granted on behalf of the State or an State guarantee, as well as remaining claims of the creditors.

If the Plan does not foresee the sale of pledged property, claims of secured creditors must be satisfied in the same rank as employment related claims (Art. 14 para. 2 LRE). Under the LRE, the same two-staged satisfaction procedure and the proportional satisfaction of creditors in a same rank apply as under the LBE (Art. 14 para. 3, 4 LRE). Voting for the Plan requires a qualified majority of all the proven aggregate amount of claims when voting takes place collectively. When voting takes place in creditors' groups, all mandatory groups must vote in favour of the Plan and within each group an affirmative vote of 2/3 of the proven aggregate amount of claims must be obtained (Art. 15 para. 4 no. 4 LRE). If during the implementation of the Plan grounds emerge to institute bankruptcy proceedings and the court receives a petition for bankruptcy, restructuring proceedings must be discontinued and bankruptcy proceedings pursuant to the LBE initiated (Art. 24 para. 4 LRE). After the implementation of the Plan, the restructuring proceedings are terminated according to the procedure set forth in Art. 25 LRE.

j) International Insolvency Law

Neither the EBL nor the LRE contain provisions addressing issues of international insolvency law. Thus, Lithuanian insolvency law is currently not equipped to properly deal with insolvency cases which have an international and/or cross-border component. In particular, as of September 2007, the current Lithuanian insolvency laws have not been harmonised with the current EU norms such as the Council Regulation (EC) no. 1346/2000 of 29 May 2000 on insolvency proceedings.[395] The Lithuanian Government appears to have recognized the need to act and has recently introduced a bill to the Parliament aiming at harmonising the Lithuanian insolvency laws with the European norms. The vote on

[395] Available at: www.iiiglobal.org/country/european_union/regulation.pdf (visited: 11 September 2007).

this bill is expected for November 2007. However, the draft is not accessible to the public.

Currently, as a rule, the EBL and the LRE are only applicable to enterprises registered in the Republic of Lithuania (cf. Art. 1 para. 2 EBL and Art. 1 para. 3 LRE) and therefore not to foreign enterprises. Some recent amendments to the EBL and LRE take indirectly account of the existence of cross-border insolvency issues, albeit only for specific insolvency scenarios. Both the EBL and the LRE were amended by adding the following limitation to their respective scope of applicability; Art. 1 para. 4 EBL and Art. 1 para. 6 LRE stipulate that "[t]his Law shall apply to the extent it does not contradict the Law on Financial Collateral Arrangements and the Law on Settlement Finality in Payment and Securities Settlement Systems."[396] The mentioned Laws contain provisions on bankruptcies with cross-border effects such as Art. 8 of the Law on Settlement Finality in Payment and Securities Settlement Systems.

Judgements of foreign courts relating to bankruptcy cases may be enforced in Lithuania only after they have been recognized by the Lithuanian Court of Appeal (Art. 809 para. 1, 818 para. 1 CCP; Art. 1 no. 2 (b) Council Regulation (EC) no. 44/2001 of 22 December 2000 on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial matters).

k) Criminal Offences in Connection with Bankruptcy

The Lithuanian law only sparsely criminalizes conduct in connection with bankruptcies. In general, it is worth noting that in Lithuania not only natural but also legal persons may be offenders under criminal law. Under Art. 208 para. 1 of the Criminal Code[397] persons face imprisonment of up to two years who deliberately fulfil their obligation towards a creditor (congruent coverage) thereby causing damage to the creditors

[396] Valstybės žinios, 2004, no. 61-2183 and Valstybės žinios, 2006, no. 61-2754. Both laws are available also in English at http://www.lrs.lt/ (visited: 11 September 2007). Note that the available English version is not always up to date.

[397] Lietuvos Respublikos Baudžiamasis kodeksas. Valstybės žinios, 2000, no. 89-2741. Not available in English language.

as a whole while the enterprise is experiencing a financial crisis and it obvious that bankruptcy proceedings must be instituted. Under Art 208 para. 2 of the Criminal Code persons face imprisonment of up to three years who deliberately dispose of the enterprises assets without being obliged to do so (incongruent coverage) and thereby cause damage to the creditors as a whole while the enterprise is experiencing a financial crisis and it obvious that bankruptcy proceedings must be instituted. Under Art. 209 of the Criminal Code persons face imprisonment of up to three years who manage an enterprise badly thus causing the enterprise's bankruptcy and causing great financial loss to creditors.[398] Further, under Art. 221 of the Criminal Code persons may be punished who, despite of a reminder by the competent authority, fail to submit the requested document related to the financial situation of the enterprise (turnover, earnings, assets etc.).

5. Summary and Perspectives

The current Lithuanian insolvency framework is deficient. The two major laws, the EBL and LRE are flawed both from a formal (e.g. the wording is not harmonised, definitions are not used continuously, restructuring procedures are to formalised to be practicable) as well as from a material viewpoint (e.g. inadequate definition of grounds for opening proceedings, long waiting periods as condition precedent for petitions of creditors, focus on liquidation, no international component).

The system suffers in particular from the existence of two separate laws, the EBL on the one hand and the LRE on the other hand. Though coming into effect on the same day, their wordings are not in line and

[398] See also Art. 2 para. 12 and Art. 20 EBL on fraudulent bankruptcy and Point 13 of the decision of the Supreme Court of Lithuania of 21 December 2001 outlining the characteristics of deliberate bankruptcy.

cause numerous questions of interpretation. Restructuring/rehabilitation of enterprises is hampered due to the overly formalistic procedure under the LRE. Restructuring/rehabilitation under the EBL is almost impossible as the consent of all creditors (plus owners and management and court) is required. Not last because of these structural problems, third party financing for restructuring/rehabilitating is almost impossible to acquire. This leads to the current situation in which restructurings under the LRE are the rare exception. Practitioners observe that the LRE is mainly used abusively to delay the opening of bankruptcy proceedings (cf. Art. 8 LRE). What is more, courts and also some administrators lack the knowledge necessary to handle effectively and efficiently this complicated material in which legal, financial and commercial aspects mingle. The absence of specialised courts for insolvency proceedings is not helpful in this regard. Overall, it can be observed that not much trust is placed in the current system.

The current initiative by the Government to amend the EBL in order to harmonise it with European norms is a first step into the right direction. Although the bill has not been made public yet, a list of those Articles was published which will be affected by the bill. Reviewing this list, it can be assumed that the Government not only intends to harmonise the EBL with the European norms but also attempts to push through additional changes. In any case, the amendment of a substantial number of Articles will not solve the structural problems summarized above. Rather, it will be necessary to draft a new legal framework which should unite the bankruptcy and the restructuring procedures under one roof, establish a specialised court branch, and take account of the international components. It might also be worth contemplating to introduce insolvency proceedings against natural persons. The German InsO might serve as a suggestion.