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THE SERVICE SUPPLIER AND ITS AVATARS REFLECTED IN THE INSOLVENCY PROCEDURE

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CHAPTER IV. SERVICE SUPPLIER AS A STATE-OWNED ENTERPRISE

ABSTRACT

Key words*: essential supplier; captive consumer; indispensable creditor; unsecured creditor; state-owned enterprise; utilities*

The opening of the insolvency procedure represents the event that metamorphoses not only the universe of the debtor subject to the insolvency procedure, but also that of the creditors it engages in its procedure. Metamorphosis generates new rules in contractual and extra-contractual relationships, even a new time with different valences for participants.

The involvement of the service suppliers in the insolvency procedures is a *sine qua non* condition, in particular during the observation and reorganization procedures. Its contribution is crucial to the insolvent debtor, being the source essential supplies for the latter's survival and revival.

Insolvency procedure often apply to a financially exhausted debtor, whose chances of recovery depend on a transfer of energy and resources that are vital to its activity. The first aid line consists

of former contractual partners, who provide services and products in the absence of which the debtor's activity is inconceivable: water, electricity, natural gas, communication services.

As a result of the defining role that essential creditors play and independently of their will, the law binds them to the insolvent debtor, marking their fate by the triple prohibition to change, refuse or temporarily interrupt the service to the debtor.

The legal framework applied to service suppliers is completed by its avatars generated by the legal provisions. From the perspective of the insolvency legislation, the service supplier is a current creditor, which does not, however, have the quality of creditor entitled to participate in the procedure, as Law no. 85/2014 defines this category of creditors; instead, a number of rights and safeguards are attached to compensate for the effort involved in accompanying the insolvent debtor in the recovery procedure.

The concept of service supplier acquires individuality in relation to the corresponding concepts in other legal systems; the mirroring of the supplier being made in the concept of essential supplier, established by the Insolvency Act 1986 or critical vendor, as outlined in the doctrine of necessity in the United States under the Banckruptcy Code.

An ontological perspective places the service suppliers in the category of state-owned enterprises, creating the premises for the application of regulations dedicated to corporate governance. The state is not a regular shareholder and could not be and this is reflected in the attitude of the service supplier during the insolvency procedure.

The legislation regulating the activity of the service supplier reveals it most often as a participant in the energy market, being subject to the provisions of Law no. 123/2012 as well as to the secondary legislation consisting in the orders of the president of the National Energy Regulatory Authority.

The challenge assumed by this paper is to determine the content of the concept of service supplier by establishing the economic operators that can be included in this category and, implicitly, which energy market participants should not be subject to the Article 77 of Law no. 85/2014. There are indications that lead to the idea that the transmission system operator or the producer of natural gas or electricity should not be considered as service suppliers within the meaning of Law no. 85/2014, although the judicial practice proved to be confusing in this respect, in the absence of sharp legal provisions.

The analysis of the condition of the service supplier from the four perspectives listed above (current creditor, energy market participant, essential supplier, state-owned enterprise) is also a test of the coherence and efficiency of the legal system.

Addressing the issue of insolvency combined with that of energy resulted from the finding of the summary and fugitive treatment applied to the service supplier as a creditor in insolvency procedure. The doctrine did not avoid the subject of the service supplier, but left enough room for challenges resulting of the insolvency legislation facing the energy legislation. The field of confrontation of the two legislations is undermined by inconsistencies that lead to confusing effects of the insolvency procedure.

Finally, to emphasize the importance of the central character of the paper, we propose a short and simple exercise of imagination: what would the insolvency procedure look like in the absence of the service supplier?

Consequently, the purpose of the following chapters is to reveal the mystery nurtured by the service supplier and, finally, to give this creditor what it deserves: a comprehensive analysis, by alternating its avatars.

The opening of insolvency procedure represents a hierophany in the collapsed universe of the debtor. Entering insolvency comes with a different flow of time (it stops, flows in the sense of decay, but also of fulfillment), thus creating a dimension that is peculiar to the insolvency procedure and which coexists with ordinary reality.

Metamorphoses also appear regarding the participants in the procedure as from contractual partners they become creditors, divided into multiple categories, some even playing the role of *Janus Bifrons*, with one part facing the past (as a historical creditor) and the other facing forward (as a current creditor).

The current creditor is inevitable in the insolvency procedures, and its legal regime is built on the legal provisions that directly apply to him, but also on the distinctive elements compared to other creditors. For example, the current creditor (or the creditor with current debts) and the creditor entitled to participate in the procedure (or the historical creditor) form an antagonistic couple in the procedure. The fact that determines the antagonism between the two concepts is the time, so that the

genesis of the historical creditor's debt is located before the date of opening the insolvency procedure, while the current creditor's debts arise after this crucial moment.

The effectiveness of the legal framework regarding the current creditor results in the ability to collect as much as possible of his debts and the position on the distribution list. The current creditor is, however, in most cases an unsecured creditor. However, it has the right to be paid on due date. Among the current creditors, the service supplier regulated by art. 77 of Law no. 85/2014 is inevitably present in any insolvency procedure. The terminological inconsistency reflected art. 77 leads to the difficulty of determining the economic operators that fall into this category of creditors; art. 77 presents three alternative concepts: "supplier", "service supplier" or "utility supplier" referring to the same creditor. Another aspect of terminological nature is the possibility of outlining the concept of supplier within the meaning of art. 77 in terms of legislation and terminology specific to the energy field, which makes a clear difference between the supplier, distributor or transmission system operator of natural gas, electricity or heating.

The case law also contributes constructively to the determination of the conceptual sphere of the creditors supplying services (utilities), the present paper presenting relevant decisions of the Constitutional Court, the High Court of Cassation and Justice, courts of appeal.

The services (and, eventually, the products) which are the object of the supplies from art. 77 are often confused with the raw materials. The difference between them is relevant because the utilities are under the legal coverage of art. 5 point 10 in conjunction with art. 77, whie the raw materials under that of art. 5 point 23 in conjunction with art. 134, the applicable legal regime being different. Examples of products that can be the subject of a utility service, but can also be a raw material are: gas, electricity, water.

Most utility suppliers find themselves in a natural or legal monopoly position and consequently are unavoidable for customers and their effort to create a portfolio of clients is reduced to minimum. In return for this privilege, utility suppliers carry out a more intensely regulated activity, which limits and stiffens the freedom of action.

The insolvency procedure upsets the order of the contractual relations *in bonis* in which a supplier is a part and turns him from privileged to captive in the insolvency procedure of his clients.

The fate of the supplier is closely linked to that of the captive consumer, defined by art. 5 point 10 of Law no. 85/2014. The legislator establishes for the service suppliers, during the period of observation and reorganization, the triple interdiction to refuse, to interrupt or change the terms of service supply in relation to a captive consumer.

The concept of 'captive consumer' is not deprived of interpretations, thus that the case-law, once again, manifests its essential role in outlining and determining the conceptual sphere.

Law no. 85/2014 proves to be more favorable with suppliers compared to Law no. 85/2006, thus contributing to the balancing of the participants' interest in the procedure by establishing several legal instruments made available to them in order to protect their rights: the possibility of interrupting the supply of services if the debts arising after the opening of the procedure are not paid; the interrupted service is supplied again only after the current debts are paid; the possibility for supplier to request the court to open bankruptcy procedure against the debtor in the event of non-payment within 60 days after the maturity of current, certain, liquid and due debts that exceed the threshold value; the possibility to use the individual foreclosure of debts accumulated during the insolvency procedure that are older than 60 days; the possibility to request a guarantee provided by the debtor for maximum 30% of the unpaid debt.

The debtor's captivity to his supplier is established on the basis of three considerations: technical, economic and regulatory, which do not have to be met cumulatively.

The category of current creditors risks to be confused with that of indispensable creditors. The indispensable creditor benefits from a legal definition contained in art. 5 point 23 in conjunction with art. 134 of Law no. 85/2014. This category of creditors has a *intuitu personae* character, being essential the quality of the creditor in relation to the debtor as well as the impact of the contractual relationship concluded between them on the activity of the insolvent debtor. Unlike other creditors, the category of indispensable creditors is created according to a procedure expressly established by Law no. 85/2014. The list containing the indispensable creditors proposed by the debtor is attached to the petition for opening the insolvency procedure and is subject to censorship by the judicial administrator.

From the point of view of the interpretation of the legal regulations, as well as of the jurisprudence, the overlap of the two categories of creditors, current and indispensable, must be avoided.

The correspondent of the service supplier within the meaning of art. 77 of Law no. 85/2014 is also found in the legislation dedicated to insolvency procedures in England, respectively in Insolvency Act 1986, and is represented by the "essential supplier", whose legal regime is similar to that established by the Romanian legislation.

Insolvency Act 1986 was amended by Order no. 989 of 2015 regarding the protection of essential suppliers, which extended the list of suppliers that have to continue providing the good or service indispensable to the debtor's activity, respectively: electricity, gas, water, telecommunications services; IT goods and services. The provisions of the Order are specific to administration and voluntary arrangements.

Contracts concluded between the debtor and the essential suppliers shall be deemed to have been maintained from the date of the opening of the procedure if the debtor or the insolvency practitioner notifies the supplier about the fact that its performance is essential to debtor's activity. In order to continue the contractual relationship, the essential suppliers are prevented from compelling the payment of charges incurred before the insolvency or to charge higher rates as a condition of continuing supply.

However, Order 989 of 2015 provides safeguards for suppliers of essential goods or services. In particular, they enable the suppliers to: terminate the supply, unless an insolvency office-holder personally guarantees the payment of any charges in respect of the continuation of the supply; terminate the contract where an insolvency office-holder consents to the termination; terminate the contract where a court grants permission for the termination if the court is satisfied that the continuation of the contract would cause the supplier hardship; terminate the contract where any charges in respect of the supply that are incurred after the company enters administration or the voluntary arrangement takes effect are not paid within the period of 28 days beginning with the day on which payment is due.

American law also benefits from the recognition of essential suppliers called either "essential suppliers", as in the Insolvency Act 1986, or "critical vendors". The legal regime of this category of creditors is considerably different from that of the essential supplier in England or Romania.The first difference as well as peculiarity is that Bankruptcy Code does not include provisions on the essential supplier/critical vendor, the case-law being the one that outlined this concept.

In the USA, the suppliers have no legal obligation to maintain their availability to continue contracts, given the non-fulfillment of payment obligations; moreover, there is no legal provision that requires forced continuation of supplies.

Under these circumstances, the debtor must identify incentives to persuade and encourage suppliers to accompany him in the reorganization process. The strongest incentive is to pay the debts prior entering insolvency, without neglecting the current debts also.

The legal basis found in case-law, around which the doctrine of necessity was built, is paragraph 105 (a) of the Bankruptcy Code. The case-law has been constantly evolving and has refined the legal regime of the essential supplier, starting from a lax interpretation, which created a real overload of this legal basis, leading to slippage. This approach was valid until the Kmart case, which determined the change of perspective and new conditions in creating the list of essential suppliers.

The courts have ruled that the use of the doctrine of necessity as a basis for approving the payment of debts prior insolvency in favor of essential suppliers must be combined with the fulfillment of the following two conditions: the creditor must provide essential goods or services for the reorganization of the debtor; favorable treatment applied to the essential supplier must not cause prejudice to other unsecured creditors.

In order to complete the image of the service supplier, the extra-insolvency perspective of this creditor should be analyzed. This complementary approach is intended to emphasize the idea of the need to design a coherent and functional legal system with correlated and effective rules.

The service supplier is in many cases a state-owned enterprise, acting especially in the field of energy. The state, through central public authorities or local public authorities, is not accidentally a shareholder / associate in these enterprises. In many of the state-owned enterprises, the state was initially the only shareholder, but the successful completion of privatization processes led to the opening of these enterprises to private investors.

The activity of state-owned enterprises is of the greatest relevance and is mainly analyzed at national level as state-owned enterprises have traditionally been designed to serve the internal market. Romania is an eloquent example for the study of state-owned enterprises as it is the country with the highest number of state-owned enterprises in Europe.

State-owned enterprises were removed from the opacity and rudimentary regulation by adopting GEO no. 109/2011. This regulation did not appear from the awareness of the Romanian legislator that there was a need to reform the field of state-owned enterprises, as, perhaps, it would have been natural. The corporate governance regulation for state-owned enterprises was stimulated by foreign incentives, consisting of Romania's international commitments and was inspired by the principles developed by the Organization for Economic Cooperation and Development.

The concept of state-owned enterprise comprises four categories of entities: autonomous government – owned enterprises; national companies and enterprises; companies where the state or an administrative and territorial unit is the unique or the majority shareholder, or where it holds control; companies where one or several state-owned enterprises hold a majority stock or a large enough stock to provide control.

The state is not a regular shareholder and could not be one. The legal status, the rationales of the state as a shareholder, its rights within the state-owned enterprises place it on another stage, which cannot be leveled in terms of ordinary shareholders' conduct.

For these reasons, it is deeply meaningful the involvement of the state in the state-owned enterprises and the relationship it develops with these enterprises.

The main goal that the state, as a shareholder of state-owned enterprises, must pursue is to maximize the value of society by efficient allocation of resources and involvement in the following levels: control over natural resources, natural monopoly, public service, strategic reasons.

In order to comply with the corporate governance provisions, the state must develop and make public its shareholding policy, designed to provide both the state-owned enterprises and the society in general predictability, a clear understanding of the objectives of the state and its priorities as a majority shareholder.

Sound corporate governance is based on the principle of real separation of the three functions that the state exercises in relation to a state-owned enterprise: the ownership function, the normative function and the function of industrial policymaker. Relevant for this paper is the ownership function, which, in the case of Romanian state-owned enterprises, is characterized by segmentation and lack of coordination at the level of line ministries. The current trend, noted in developed

countries, is to centralize the function of state ownership within a single entity or a very small number of entities.

The dividend policy is relevant both for the state, as state-owned enterprises are considered a vector of economic recovery and budget balancing, as well as for private investors, whose interest is very sensitive to the gain they can get from investment. Typically, state-owned enterprise that distribute and pay dividends to the state budget are overwhelmingly national companies.

The general perception regarding the financial results and the evolution of state-owned enterprises, is not a positive one, state-owned enterprise being classified as a burden on the public budget. The most profitable public enterprises stood out in the production and supply of electricity and heat, gas, hot water and air conditioning or pipeline transport.

Despite a decade of corporate governance regulation of state-owned enterprises in Romania, the implementation of corporate governance mechanisms is unsatisfactory, with room for improvement in the establishment of corporate governance structures by public authorities, in starting and finalizing the selection procedures of the members of the board of directors / supervisory board, of the directors / directorate.

Internationally, countries such as China are present in the top of the largest state-owned enterprises, followed by India, Russia and the United Arab Emirates, Malaysia.

At European level, state-owned enterprises play a decisive role especially from the perspective of the following aspects, which overlap with those identified in Romania, namely the number of jobs involved, the representation in GDP of state participations in state-owned enterprises and the fields these enterprises predominate.

Another avatar of the service supplier is outlined in the analysis of the history of gas legislation and insolvency legislation. It results that, from a temporal point of view, the two areas of law developed in parallel, ignoring each other.

The challenges brought by the insolvency procedure in the field of energy legislation are highlighted by the way contracts are executed, by the challenges that the contractual relationship between the transmission system operator and the network users experience when facing insolvency.

The principles of freedom of contract and autonomy of will are minimized when concluding a natural gas transmission contract as they strictly show up when parties make the decision to conclude the contract, given that the contractual clauses are imposed by a third party: the National Energy Regulatory Authority. The contract is a standardized one, the variables within it being limited to the agreed capacity product (annual, quarterly, monthly, daily, intra-daily), which automatically sets the duration of the contract and how the financial guarantee of payment is given by the network user.

As a result of the inadequacy of the insolvency legal framework to provisions in the natural gas field there are several insolvency mechanisms that are either diverted from their purpose or their implementation takes a less expected turn.

Termination of contracts, although may seem the desire of any creditor, is not always advantageous for the service supplier. The disadvantages consist in the non-fulfillment of its regulated income, according to the legal provisions, and the impossibility of recognition in the service tariff of the debts not recovered following the bankruptcy procedures. Moreover, termination of the contract is a real challenge for the supplier as proving the fault of the insolvent debtor for non-payment of debts is not easy, the lack of liquidity being a common matter once entering insolvency procedure.

Both in the insolvency procedure and in the electricity and natural gas law, there are safeguard institutions for the service supplier: the guarantee regulated by art. 142 of Law no. 85/2014 and the financial payment guarantee provided by art. 27 lit. A of the Network Code. Although, apparently, both have the same object, the guarantee and the financial guarantee of payment can be cumulated especially when the debtor-user of the network does not restore the guarantee after a partial execution or does not constitute it at all.

The terminology used in the two areas of law should be uniform, ensuring the coherence and efficiency of the legal system. However, numerous terminological arguments from Law no. 123/2012 do not fully respect the spirit of Law no. 85/2014 or vice versa. The provision of the Order of the National Energy Regulatory Authority no. 41/2019 upsets, however, the construction of arguments that tend to create an equivalence between the supplier regulated by art. 77 of Law no. 85/2014 and the supplier, participant in the natural gas or electricity market, regulated by Law no. 123/2012.

In order to protect the service supplier, but also as a way of terminating the contract, Law no. 85/2014 allows more efficient instruments to determine the debtor to pay current debts. Thus, in case of non-fulfillment of the payment obligation within 90 days, the utility supplier may interrupt the provision of the service until it receives the due payment. In addition, the observation period has also reduced its rigidity, so that the unpaid supplier may file a bankruptcy motion against the debtor at this stage of the procedure as well.

The changes brought by the new insolvency law are also echoed in the field of natural gas. It is noted the presence of changes in the institutions already existing in Law no. 85/2006, as well as new institutions, positively perceived by the participants to the energy market. Of these, the highest frequency and impact have the following elements: the sanction for non-payment of current debts, the limits set for the observation period, the motion for establishing the existence and/or the amount of a current debts, the individual foreclosure and the legal set-off.

The exposure of the captive service supplier in its debtor's insolvency procedure was limited by the provisions of art. 77 para. (4) of Law no. 85/2014, which unequivocally establish that if the debtor does not pay the debts arising during the insolvency procedure, related to the service supplies, within the payment period which may not be less than 90 days, the utility supplier is entitled to interrupt the provision of services. In addition to the above, para. (5) of the same article states that the provision of the service will be resumed after the payment of current debts.

The time limit set for the observation period is welcomed by creditors. This measure is intended to avoid the unreasonable temporal extensions of the observation period and the undermining of real chances for debtor's recovery.

The exception to the suspension of all legal proceedings, extrajudicial proceedings, foreclosure consists in the right of current creditors to file the petition to determine the existence and /or amount of current debts.

With the effect of a revolution in the philosophy of Law no. 85/2014, the individual foreclosure within the insolvency procedure was introduced with the stated purpose of favoring the efficiency of the mechanisms for recovering the budget debts. However, theoretically, the provisions of art. 143 para. (1) may benefit to any creditor who meets the requirements established by the common law, thus making possible anti-economic behaviors and against the discipline that Law no. 85/2014

dictates to creditors. The doctrine reacted strongly to the introduction of this institution in the insolvency procedure, calling it against the reason of the law and even unconstitutional.

Another controversial legal institution in the insolvency law is that of legal set off, regulated by art. 90 of Law no. 85/2014. Its compatibility with the insolvency procedure, the right to waive compensation, as well as the creditors who may use it were the subject of the notification of the High Court of Cassation and Justice, which ruled by Decision no. 19/2020, clarifying the aspects that generated a non-unitary practice.

The last years (starting with 2014) have demonstrated an intensification of insolvency procedure in the field of energy, the most affected participants in the energy market being the suppliers and distributors. Thus, the service supplier becomes himself a debtor in insolvency procedure.

The need to establish special provisions, dedicated to the energy supplier as a debtor, results from the specific activity it carries out, which once faced with insufficient funds to pay certain, liquid and due debts, needs deviations from the common legal regime in order to achieve the purpose of the procedure.

The areas that already benefit from a special regime in insolvency procedure are: banking, groups of companies and insurance / reinsurance companies.

The field of energy arouses intense interest due to the resources it manages. This interest is amplified by the need to fulfill legal and contractual obligations towards final consumers. Most of the activities carried out by energy companies are public services, and this implies a special status and specific obligations.

In conclusion, this is the picture of the service supplier and its avatars activated by the spectrum of different laws. The service supplier is an indispensable creditor to the insolvency procedure, which belongs to the category of current creditors. The service supplier, seen in the depth of the history of its existence, reveals itself under the regime of a state-owned enterprise, but also as a participant in the energy market as a result of the decentralization of state control over energy entities.