Dimitar Gelev[1]*, PhD*

Insolvency Proceedings and Court Payment Orders – Legal Problems

Abstract

This paper deals with the treatment of court payment orders in connection with domestic insolvency proceedings.

At the outset the paper presents some general legal problems connected with the legal definition of the term "trader" or "merchant" in order to define the circle of persons covered by the provisions of insolvency regulations. After brief explanation of the court proceedings for the issuance of payment orders, the paper further analyzes practical problems connected with execution of payment orders in accordance with the status of the debtor and in connection with the opening of insolvency proceedings.

In conclusion the author proposes complete reform of domestic laws and regulations which deals with this issue, because he believes that they are completely outdated and do not correspond with reality.

Keywords: insolvency, payment order, court payment order, compulsory execution proceeding, insolvency proceeding, payment services provider, payment services user

In the former Insolvency Law of the Republic of Macedonia there were three bases for the opening of the insolvency procedure: (1) insolvency (or illiquidity), (2) imminent insolvency and (3) over-indebtedness.[2]The bases referred to under (2) and (3) were especially relevant in respect of the "subjective test" of standards for conduct of the debtor and his criminal liability, but these two bases were abolished in the subsequent versions of the Law.

The current version of the Insolvency Law contains only one reason for initiation of the insolvency procedure: illiquidity, defined as inability to pay offa debt due in the period of 45 days.[3]Under the Law, natural or legal persons may be subjected to the insolvency procedure,while under the term "natural person" the Law on Commercial Companies understands only a sole merchant (and not for example members of partnerships or members of limited partnerships with unlimited liability), which is a very strange concept. In all civil law countries, members of personal commercial companies are also considered merchants (except limited liability partners in a limited partnership).[4]

---

[1]Dimitar Gelev, PhD – Professor at the Department of Business Law and Economic, Faculty of Law "Iustinianus Primus", University "Ss. Cyril and Methodius, Skopje, Republic of Macedonia.

[2]See: Insolvency Law, Off. Gazz no 55/97.

[3]See: Insolvency Law, Off. Gazz no 34/06, 126/06, 84/07, 47/11 and Decisions of the Counstitutional Court U no. 63/06, 11/09.

[4]See: Law on commercial companies, Off. Gazz no 28/04, 84/05, 25/07, 87/08, 42/10, 48/10, 24/11, 166/12.

A precise definition of the term "merchant" or "trader" is very relevant for the definition of the circle of persons which may be subjected to the insolvency procedure. In most civil law countries, compulsory execution procedure is used for all those persons that are not regarded as "merchants" (and are treated as ordinary citizens) and insolvency procedure is relevant for all those which are defined as such (as "merchants"). The German Insolvency Act which was a basis for the first version of the Macedonian Insolvency Law uses the terms "natural and legal persons" (and not merchants) because this Act introduces a procedure for "consumer insolvency", which is not the case with the Macedonian Law.[5]Today the Macedonian Insolvency Law and other related laws have no precise definition of the term "merchant" which leads to a very vague notion of the circle of personsthat may be subjected to the insolvency procedure.

Some other domestic laws applied definitions of merchants to persons that traditionally are not regarded as such: like artisans, architects, engineers, accountants etc., even to the "artists".[6]

This vague (and very often ridiculous) definition of the term "merchant" is additionally complicated when we come to the procedure of issuing court payment orders.Notwithstanding the procedure for issuance of the payment order, further destiny of the issued order (even with the seal of enforceability) largely depends on the status of the debtor. If this person has a status of civil person (person under the civil law), normal compulsory execution procedure will apply. But if the debtor has a status of merchant (trader), inability of enforcement of the issued enforceable payment order will lead to opening of insolvency procedure. As I said before: illiquidity is now the only legally recognized ground and reason for the opening of the insolvency procedure in accordance with the domestic law. If a person who has an executable payment order cannot obtain execution from the debtor's bank account, he normally must apply before the court for opening of the insolvency procedure against the debtor. But is this the case in Macedonia?

First I will briefly analyze the legal norms in respect of issuance of the payment order. Traditionally in Europe there existed two forms of "payment order procedure": "evidence models" and "no evidence models". The evidence model implies that the claimant must produce documentary evidence to the court in order to substantiate his claim. In this model the main purpose for requesting documentary evidence is protection of legal and procedural position of the debtor. On the contrary, "no evidence model" implies that the claim is based on the mere statement of the claimant, which is subject to suspension until the debtor has not demonstrated the contrary. This means that in this model there exists an implicit ("alleged" or "presumptive") judicial protection, as a certain degree of trust is granted to the claimant, who wants to be protected from a possible economic prejudice.

The first mentioned model ("evidence model") had been a dominant model in the European civil law countries before adoption of

[5]See: German Insolvency Statute of 5 October 1994, Federal Law Gazzete I page 2866, as last amended by Article 19 of the Act of 20 December 2011, Federal Law Gazzete I page 2854.

[6]See: Law on construction, Off. Gazz no 130/09, 124/10, 18/11, 36/11, 54/11, 13/12, 144/12, 25/13, 79/13; Law on artisans, Off. Gazz no 55/07.

Regulation (EC) 1896/2006 (mainly based on the German and Austrian legal practice).[7]

The difference between the two models is easily understood.In the "evidence model" the claimant will provide all the necessary documents with the aim to prove that he really has a claim against the debtor. In the "non evidence model", a debtor must supplyproof to the contrary, of the non-existence of the claim, if he wants to demonstrate that he is not responsible.

A debtor may react on time when he receives a payment order or notice of enforceability for the payment order and initiate a regular legal court procedure.

Due to the total absence of political will for reorganization of the former socialist Social accountancy or bookkeeping service (SOK) or later the Payment Bureau (ZPP), the process of stripping the courts of their competencies started in Macedonia. This process could be seen in the procedure for registration of tradersand commercial companies (merchants) and other associations and legal entities, and later in the procedure for registration of rights overthe immovables (land register). The same tendency now is also seen in the procedure for issuance of the payment orders. This process is also accelerated by the total absence of political will for acceptance of modern technologies (computers and automated systems) in the regular work of domestic courts. In this respect, they lag behind for a decade or more. All this is appropriately reflected in some outdated court procedures, for instance, in respect of issuance of payment orders. And again, the legislature and executive government instead of computerizing courts in the country took the easiest way. They retain outdated court procedures and transfer court jurisdictions to other state organs or even to public notaries, thus creating a big mass. For the legislature, it is easier to invent new unknown instruments (like "zadolznica" no translation possible) unknown in the civilized world, just not to reform the already outdated court procedures.

For instance if we look at the German summary proceedings for issuance of payment orders regulated in Book 7 of the German Code of Civil Procedure (asa similar civil law pattern), we will notice a very big difference (especially in issuance of court payment orders in "no evidence model").[8]There they have a routinized procedure which uses automated system with no human interference in most cases and a procedure with appropriate forms and technology, which is far away from our reality. In our reality everyone has court jurisdiction (payment services, banks, some financial societies, even public notaries, but court jurisdiction is reduced to a minimum. All the explanations that in that way we facilitate payments in the country, that this is necessary for the electronic process or that in this way we made the work of overburdened courts in the country easier are ridiculous. But all available statistics clearly indicate that this is simply not true.

[7]Regulation (EC) 1896/2006 of the European Parliament and of the Council of 12 December 2006 creating the European order for payment procedure, OJ L 399 30/12/2006.

[8]See: German Code of Civil Procedure as promulgated on 5 December 2005, Bundesgesetzblatt, I page 3202; 2006 I page 431; 2007 I page 1781; last amended by Article 1 of the Act dated 31 August 2013, Bundesgesetzblatt I page 3533.

For a detailed plastic description of the German court procedure for issuance of payment orders, I will refer to the short work of GrozdanaŠijanski and Jimmy Barber – "The German order for payment procedure (*Mahnverfahren*)" and I will not analyze this procedure any further.[9] But we must note that in "no evidence model" court payment orders have everywhere a status of default judgment (or in our terminology "judgment made in absence of the other party"), which seems is not the case in our procedure, becausein our procedure it seems that this payment order is treated like judgment in meritum (which is strange).

Here I will just mention that a payment order is a legally regulated device and international banking term that refers to a directive to a bank or other financial institution from a bank account holder instructing the bank to make a payment or series of payments to a third party. It can be defined as instructions to transfer funds sent via paper and/or electronic means. In our domestic law this is generally regulated by the Law on Obligations (Part XXI and some other specific provisions) and in some contradictory way in the Law on Payment Services, and here the only difference being that a payment order is issued by the court, and not by "bank account holder" for some specific purpose and with appropriate legal ground in the phrase of execution of the court orders in general (and is treated as a kind of judgment executed as any other court judgment).[10]

However, my specific interest here is not the court procedure for issuance of payment orders, but their destiny when they come to the phrase of execution and specificity of that execution according to the status of debtor: civil person (ordinary citizen) or merchant (trader). As we know, almost all civil law countries have some kind of division of private law into civil and commercial law (with distinct features for registration, transactions, interest, protection, even separate court systems etc.). This was not the case in almost all common law countries. But in civil law jurisdictions this distinction is somewhat blurred after acceptance of separate procedures for consumer insolvency, modeled mainly on the American pattern. This American pattern traces its roots in old codes like Justinian Institutions as they are receipted in the common law world and are very similar to procedures for guardianship. But if some form of insolvency is accepted for ordinary citizens (mainly for the bank credit cards), this has a very big influence on legal definitions in insolvency codes or laws. The procedure for "consumer insolvency" is far from real insolvency procedure for merchants (real bankruptcy). In general, all civil law countries still maintain a distinction between compulsory execution proceedings for ordinary citizens and insolvency and bankruptcy procedure for merchants.

In practical terms this means that if the debtor is an ordinary citizen he may apply for "consumer insolvency" (if this is provided by the legal system of the country) or otherwise normal rules of compulsory execution proceedings are applied. But if the debtor is a merchant and a

[9]Shijanski G. & Barber J. (2006), "The German order for payment procedure (Manhverfahren)", Pauline V. and © 2006 Gerhard D, http://www.iuscomp.org/gla/literature/sijanski.htm

[10]See: Law on Obligations, Off. Gazz no 18/01, 4/02, 5/03, 84/08, 81/09, 161/09 and Decisions of the Counstitutional Court U no. 121/01, no 67/02.

payment order may not be executed on the bank account of the debtor, creditor must apply for opening of the insolvency (bankruptcy) procedure.

In this respect all countries with automated and simplified systems for issuance of payment orders have special rules in their insolvency statutes about the consequences of that opening in respect of issued payment orders.

When seen from the perspective of the debtor,for example article 21 of the German Insolvency Act enumerates powers of the insolvency court which may "take all measures appearing necessary to avoid any detriment to the financial status of the debtor for the creditors until the insolvency court decides on the request" (for opening of the insolvency procedure). Among the measures, the Act mentions appointment of a provisional insolvency administrator, appointment of a provisional creditor's committee, imposition of a general prohibition on making dispositions on the debtor, order of provisional interception of the debtor's mail and most importantly court may order a prohibition or provisional restrictions on measures of execution against the debtor (unless the immovables are involved).But the German Act exempts some payment orders and financial securities from this, especially when they are handled through automated or electronic systems. This exception mainly stems from the general legal provision (repeated once again in the German Insolvency Act that any mandate ordered by the debtor referring to the property forming part of the insolvency estate expires upon opening of the insolvency proceedings, but that this provision shall not apply to payment orders or to orders between payment service providers or intermediary bodies and orders for the transfer of securities, because these shall continue to exist with effect for the assets.[11] Similar provisions are contained in the domestic Law on Obligations (Chapter XXI, articles 805 et seq) and in the domestic Insolvency Law (for example article 167), but in shortened form and with no reference to the payment system providers or intermediary bodies. The domestic Law on Civil Procedure also contains scarce provisions in this respect.[12]

But when this problem is seen from the perspective of the creditor, the situation is somewhat different. If a creditor has an executable payment order and if the debtor has no available amounts of money on the bank accounts for payment of the debt for which a court order is issued, instead of applying for the insolvency procedure(if the debtor has a status of merchant), our creditors proceed with normal compulsory execution proceedings, as in case of ordinary citizen or as nothing happened with respect of debtor's insolvency.

The domestic Law on Payment Transactions authorizes domestic banks and branches of foreign banks licensed for payment services providers and the Central Bank and the State Treasury to execute issued court ordersin respect of bank account which they opened for their clients (article 6) or for budgetary users (articles 7 – 9). All relevant provisions about the priorities and proceedings in respect of payment orders (including the court issued paymentorders) are mentioned in articles 21 and 22 of the above-mentioned Law and article 24 (obligation

[11]German Insolvency Statute, op.cit. Articles 115, 116.
[12]See: Law on Civil Procedure, Off. Gazz no 79/05, 110/08, 83/09, 116/10, 7/11.

of payment service provider to inform the Central Registry that the account of a user of payment services is blocked for more than 45 days, with appropriate fine if this is not done).[13]

When a comparison is made between this system and systems in any other civil law country with some normal market economy, one must notice that all these "payment procedures" are nothing but just a cover-up of the former communist regimes for payments and that the so-called computerization is just an excuse for that situation. If there are no clear rules for elementary things like who has a status of merchant and who has not, what procedure is relevant for merchants and what for ordinary citizens and what are the consequences of illiquidity of 45 days (which is actually in only disposition of the Central Registry), possibilities for abuses are limitless. If we look in the law which regulates the Central Registry, we will find no provision about this issue at all.[14] So we come to the situation "minister says so" which is "very democratic state of things" and "fundamental precondition for the Rechtsstaat".

The same state of affairs, we may find in the provisions of the Penal Code of the Republic of Macedonia.[15] For example, in accordance with the German Insolvency Act when the legal person or partnership becomes illiquid or over-indebted, members of the board of directors or the liquidators or other representatives must file a request for the opening of insolvency proceedings without a culpable delay, at the latest three weeks after the commencement of insolvency or over-indebtedness. If they do not file a request for the opening of proceedings, do not correctly file a request or do not file a request in good time, they shall be punished with imprisonment for not more than three years or a fine (or no more than one year or a fine if they act negligently).An analogous provision in our domestic Law is found in article 355 of the Insolvency Law which prescribes a fine of 1000 to 2000 euros for the same thing (but the obligation is prescribed as filing a request in 21 days from the commencement of illiquidity). Or we find an extremely ridiculous provision about the "responsible person of sole merchant" (which just proves that the domestic legislator does not at all understand some basic legal categories).

If we later on compare provisions of our Penal Code with the provisions of, for example,the German Criminal Code, we must see the difference.[16] As theory says no person shall be guilty only because he is insolvent. There must be some form of intent for defrauding creditors or some form of negligence in respect of the standards of professional behavior (good trader or merchant etc.). But when all this is resumed to 45 days of insolvency which is known only to the Payment Bureau or the Central Registry, things became interesting. Especially in the country with very vague rules in respect of bookkeeping and accountancy.

---

[13]See: Law on Payment Transactions, Off. Gazz no 113/07, 22/08, 159/08, 133/09, 145/10, 35/11, 11/12, 59/12, 166/12.

[14]See: Law on Central Registry, Off. Gazz no 50/01, 49/03, 109/05, 88/08, 35/11.

[15]See: Penal Code Off. Gazz no. 37/96, 80/99, 4/02, 43/03, 19/04, 81/05, 60/06, 73/06, 7/08, 139/08, 114/09, 51/11, 135/11, 185/11, 142/12, 166/12, 55/13 and Decisions of the Constitutional Court U no 22/00, 210/01, 228/05.

[16]See: German Criminal Code, Federal Law Gazette I page 3322, last amended bu Article 3 of the Law of 2 October 2009, Federal Law Gazette I page 3214.

This is also seen in the basic definitions of domestic Insolvency Law which totally inaccurately defines asset, insolvency asset and insolvency mass and provide careless double or triple different definitions for terms such as netting or collateral.

Conclusions

Taken altogether, it now becomes obvious that at the start of the privatization process in the country and reforms in the former communist economic system, some political structures made a decision to make a change without a change. This is seen in the retention of the all-powerful status of the former Payment Bureauwhich gradually replaces courts and court jurisdictions. All this is explained with the need for computerization, authomatisation, centralizing of all registries etc., but every educated lawyer knows that this is just not the truth. Behind all this stays the same will for dominance in society without any rule of law. So reorganization and transformation of this system is at start and after 20 years of transition. The legal system is ruined just for money and for the status of one powerful institution which serves every government “as they please”.

Courts in this country are not ideal. Judges in this country are not ideal. But stumbling of the court system and the laws in the country starts from the desire of political elites to control everything without any control, with very vague legal norms about anything. I am a firsthand witness of this process and the role of the “foreign consultants” in it.

Today’s provisions of the Code of Civil Procedure, Law on Compulsory Execution Proceedings, Insolvency Law, Penal Code, Law on Commercial Companies, Law on Payment Services etc. are totally outdated to cope with the reality. They are made so. Today we are in the same position as at the start of our privatization and economic reforms. Nowhere. There must be a new reform of all different laws but now there is no political will for a change, nor any motivation for that. On any part.

Skilled law practitioners may tellthis story from different aspects. Court payment orders are just one.

References:

1. German Insolvency Statute of 5 October 1994, Federal Law Gazzete I page 2866, as last amended by Article 19 of the Act of 20 December 2011, Federal Law Gazzete I page 2854

2. German Criminal Code, Federal Law Gazette I page 3322, last amended bu Article 3 of the Law of 2 October 2009, Federal Law Gazette I page 3214

3. German Code of Civil Procedure as promulgated on 5 December 2005, Bundesgesetzblatt, I page 3202; 2006 I page 431; 2007 I page 1781; last amended by Article 1 of the Act dated 31 August 2013, Bundesgesetzblatt I page 3533

4. German Civil Code, Federal Law Gazette 2002 I page 42, 2003 I page 738, last amended by Article 4 para. 5 of the Act of 1 October 2013, Federal Law Gazette I page 3719

5. Insolvency Law, Off. Gazz no 55/97

6. Insolvency Law, Off. Gazz no 34/06, 126/06, 84/07, 47/11 and Decisions of the Counstitutional Court U no. 63/06, 11/09

7. Law on commercial companies, Off. Gazz no 28/04, 84/05, 25/07, 87/08, 42/10, 48/10, 24/11, 166/12

8. Law on construction, Off. Gazz no 130/09, 124/10, 18/11, 36/11, 54/11, 13/12, 144/12, 25/13, 79/13

9. Law on artisans, Off. Gazz no 55/07

10. Law on Civil Procedure, Off. Gazz no 79/05, 110/08, 83/09, 116/10, 7/11

11. Law on Payment Transactions, Off. Gazz no 113/07, 22/08, 159/08, 133/09, 145/10, 35/11, 11/12, 59/12, 166/12

12. Law on Central Registry, Off. Gazz no 50/01, 49/03, 109/05, 88/08, 35/11

13. Law on Obligations, Off. Gazz no 18/01, 4/02, 5/03, 84/08, 81/09, 161/09 and Decisions of the Counstitutional Court U no. 121/01, no 67/02

14. Penal Code Off. Gazz no. 37/96, 80/99, 4/02, 43/03, 19/04, 81/05, 60/06, 73/06, 7/08, 139/08, 114/09, 51/11, 135/11, 185/11, 142/12, 166/12, 55/13 and Decisions of the Constitutional Court U no 22/00, 210/01, 228/05

15. Regulation (EC) 1896/2006 of the European Parliament and of the Council of 12 December 2006 creating the European order for payment procedure, OJ L 399 30/12/2006

16. Shijanski G. & Barber J. (2006), "The German order for payment procedure (Manhverfahren)", Pauline V. and © 2006 Gerhard D, http://www.iuscomp.org/gla/literature/sijanski.htm