

## ENTERPRISE BANKRUPTCY IN LITHUANIA

Aldona Garškienė<sup>1</sup>, Kristina Garškaitė<sup>2</sup>

*Vilnius Gediminas Technical University, Saulėtekio al. 11, LT-10223 Vilnius-40, Lithuania*

*E-mail: <sup>1</sup>ald@vv.vtu.lt; <sup>2</sup>vfsev2@vv.vtu.lt*

*Received: 30 Sept 2003; accepted 15 Nov 2003*

**Abstract.** Since the re-establishment of the independence, Lithuania has undergone major changes in the sphere of economy and had to re-orientate it towards a new (economic) market system, to enter new markets, and to restructure the economy. The shift in business conditions has given rise to numerous upheavals, including the bankruptcy of enterprises, which had detrimental economic and social consequences (one of such evils was increasing unemployment). However, it is also necessary to point out the positive role of the bankruptcy, which is related to a growing competition in the contemporary market economy and the acceleration of changes allowing the best companies alone to survive on the market. A positive improvement in the legal basis of bankruptcy and restructuring leaves the hope that the number of bankrupt companies will decrease. Moreover, in order to reduce the bankruptcy risk, it is necessary to create a system of bankruptcy prevention.

**Keywords:** enterprise bankruptcy, enterprise bankruptcy statistics in Lithuania, legal basis of enterprise bankruptcy and restructuring, bankruptcy risk, bankruptcy prevention.

### 1. Introduction

Since the re-establishment of the independence, Lithuania has undergone major changes in the sphere of economy and had to re-orientate it towards a new (economic) market system, to enter new markets, and to restructure the economy. The shift in business conditions has given rise to numerous upheavals, including the bankruptcy of enterprises, which had detrimental economic and social consequences (one of such evils was increasing unemployment).

The bankruptcy of companies was and still is treated rather controversially in Lithuania. Enterprise bankruptcy in developed countries is a common economic phenomenon, which is an inseparable part of market relations providing a stimulus for technical, manufacturing, and social advance. The companies which are unable to compete for the realisation market of their products become bankrupt, while others start their activity. The institution of bankruptcy proceedings has become a usual phenomenon in Lithuania helping to solve the problems of different companies. It is timely instituted bankruptcy proceedings rather than the protraction of the institution of such proceed-

ings that can help a company to recover or to solve its problems with minimum losses.

The present article looks at the problem of enterprise bankruptcy in the Lithuanian economy. A generalised bankruptcy statistics allows to reveal a considerable number of advantages and disadvantages of this phenomenon.

Aim of the research - to analyse the enterprise bankruptcy statistics as well as to generalise the data and present the characteristics of bankruptcy in Lithuania.

Object of research – enterprise bankruptcy in Lithuania.

Methodology of research – analysis of statistical data and generalisation of scientific literature.

### 2. Enterprise bankruptcy statistics

The bankruptcy of enterprises is a complex economic, social, and legal process. A lot of scientific literature is devoted to analysis of such questions as causes of bankruptcy and links of strategy to financial planning [1–3], different patterns of bankruptcy laws [4], its' procedures and case studies [5].

The Republic of Lithuania law on corporate bankruptcy has within a relatively short period of time “survived” as many as three main editions and amendments. The first Enterprise Bankruptcy Law entered into force on October 15, 1992, the second – on October 1, 1997, and the third and currently the last one entered into force on July 1, 2001 [6–8]. Since 1993, when bankruptcy proceedings were instituted for the first time, all the participants of this process have already accumulated considerable experience, which allows to make certain generalisations and to discuss some problems.

Since 1993 until January 1, 2002, 1606 enterprises and 14 banks have been declared bankrupt. Bankruptcy procedures have already been completed in 453 companies [9], out of which 424 companies have been liquidated, 4 reorganised, 9 sanated, and in the case of the remaining 16 bankruptcy proceedings have been suspended or composition with creditors has been reached. Bankruptcy procedures are in progress in 1153 enterprises and 14 banks. 953 companies are being liquidated, 3 are being reorganised, 3 are being reanimated, and 194 companies are yet waiting for a decision on the bankruptcy procedure. At the beginning of 2002, restructuring was taking place in 2 enterprises and 30 companies were preparing for this procedure. The number and duration of enterprise bankruptcy procedures are presented in Table 1 [9].

These data show a firm tendency of the increase in the number of enterprises in bankruptcy by 1,4-1,7 times each year. This growth has been the most noticeable for the last 3 years. Only in 2001 bankruptcy procedures were started in 591 companies, out of which 17 enterprises had their bankruptcy

procedures completed the same year, and in the remaining 574 these procedures are being continued. In total, in 2001 bankruptcy procedures were completed in 238 companies. The analysis of the duration of the bankruptcy process in enterprises in bankruptcy and bankrupt enterprises shows that there remain a considerable number of protracted bankruptcy procedures, which were started more than three years ago (in 1993-1998). At the end of 2001, the bankruptcy processes that started in the period of 1993-1998 were still in progress in 147 companies. However, bankruptcy processes are accelerating thanks to the implementation of a new Enterprise Bankruptcy Law, which entered into force on July 1, 2001. Compared with 2000, in 2001 the number of bankruptcy procedures in progress more than doubled. Currently, a bankruptcy process lasts as a rule for two (in 42 per cent of cases) or three (30 per cent) years [10].

Over the period of 1993-2001, judicial procedures were carried out in 1127 enterprises (97,7 per cent of all the bankruptcy proceedings), while extra judicial procedures were carried out in as few as 26 enterprises (2,3 per cent of all the bankruptcy proceedings). It seems that the percentage of judicial bankruptcies is rapidly growing.

Over the entire period from 1993 to December 31, 2001, the majority of bankruptcy procedures were started in the Kaunas and Vilnius districts (Table 2). The proceedings instituted in the Kaunas district make up approximately 27,7 per cent of all the enterprise bankruptcy proceedings instituted in Lithuania, while those instituted in the Vilnius district account for 20,5 per cent.

**Table 1.** Number and duration of enterprise bankruptcy procedures (as of January 1, 2002)

Year	Started	Completed										Currently in progress
		1993	1994	1995	1996	1997	1998	1999	2000	2001	Total	
1993	6	4									4	2
1994	27			7	1	1	2	3	1	2	17	10
1995	36			1	3	2	3		5	6	20	16
1996	79				2	10	9	11	12	7	51	28
1997	108					4	18	15	10	10	57	51
1998	98						2	15	26	15	58	40
1999	247							1	42	85	128	119
2000	414								5	96	101	313
2001	591									17	17	574
Total	1606	4	0	8	6	17	34	45	101	238	453	1153

**Table 2.** Enterprises in bankruptcy and bankrupt enterprises in 1993-2001 according to districts

Districts	1993–2001			2001		
	Bankruptcy procedures started	Bankruptcy procedures completed	Bankruptcy procedures in progress	Bankruptcy procedures started	Bankruptcy procedures completed	Bankruptcy procedures in progress
Total	1606	453	1153	591	17	574
Alytus	94	30	64	34	4	30
Kaunas	445	131	314	163	7	156
Klaipėda	140	30	110	51	1	50
Marijampolė	64	18	46	15	–	15
Panevėpys	135	51	84	63	3	60
Šiauliai	171	49	122	51	2	49
Tauragė	32	15	17	11	–	11
Telšiai	139	35	104	59	–	59
Utena	57	18	39	24	–	24
Vilnius	329	76	253	120	–	120

In 1993-2001, enterprises in bankruptcy and bankrupt enterprises were predominantly trading (35,1 per cent) and industrial (34,9 per cent) companies (Table 3) [9]. In total, these companies make up 70 per cent of all the enterprises in bankruptcy and bankrupt enterprises. The percentage of trading companies in bankruptcy as compared with all the enterprises in bankruptcy is steadily growing each year, whereas that of industrial companies is decreasing by several per cent. Construc-

tion companies constitute 10 per cent of all the enterprises in bankruptcy and bankrupt enterprises, while the companies operating in the field of agriculture account for 7 per cent. Although the number of the enterprises employed in this type of activity is increasing, their percentage as compared with the total number of businesses in bankruptcy remains roughly the same.

**Table 3.** Enterprises in bankruptcy and bankrupt enterprises over 1993-2001 according to their activities

Codes of classification of economic activities	Types of activity	1993–2001			2001		
		Bankruptcy procedures started	Bankruptcy procedures completed	Bankruptcy procedures in progress	Bankruptcy procedures started	Bankruptcy procedures completed	Bankruptcy procedures in progress
	Total	1606	453	1153	591	17	574
0–14	Agriculture, cattle-breeding, fishing, coal-mining	110	33	77	42	2	40
15–37	Manufacturing	560	157	403	181	5	176
40–42	Electricity, gas, and water supply	4	2	2	–	–	–
45	Construction	169	51	118	58	–	58
50–52	Wholesale and retail trade	564	148	416	239	8	231
55	Hotels and restaurants	40	15	25	15	–	15
60–64	Transport, storage and communication	60	17	43	20	–	20
65–67	Financial intermediation	16	7	9	2	–	2
70–75	Real estate, renting and business activities	46	11	35	17	–	17
80	Education	1	–	1	1	–	1
85	Health and social work	4	–	4	2	–	2
90–93	Other community, social and personal service activities	32	12	20	14	2	12

The main initiators of bankruptcy proceedings in 2001 were town and regional divisions of the State Social Insurance Fund Board, which initiated 184 bankruptcy proceedings (31,1 per cent of all the applications to initiate bankruptcy proceedings) and the heads of the administration of enterprises, who initiated 122 bankruptcy proceedings (20,6 per cent). A similar situation was also recorded earlier. The structure of the initiators of enterprise bankruptcy processes over 1993-2001 is showed in Table 4 [9].

The creditors' claims (or financial obligations of companies to their creditors) in all the enterprises in bankruptcy and bankrupt over 1993-2001 were in excess

by 2,8 times of the value of the assets of these enterprises. The analysis of data on the ratio of the assets of the enterprises to the creditors' claims allows to conclude that the assets of all the enterprises in bankruptcy and bankrupt enterprises as of December 31, 2001 made up as little as 35,5 per cent of all the creditors' claims.

The data on the financial situation of enterprises in bankruptcy and bankrupt enterprises in separate spheres of activity are presented in Table 5 [9, 10]. The worst situation was in health and social work companies. The assets of these enterprises made up as little as 3,7 per cent of the financial obligations of

**Table 4.** Initiators of enterprise bankruptcy process over 1998-2001

Initiators	Number of enterprises			
	1998	1999	2000	2001
Total	98	247	414	591
Employees	2	3	4	4
State Social Insurance Fund Board	11	69	145	184
State Tax Inspectorate	6	9	31	54
Proprietor (proprietors)	8	27	25	27
Shareholders, stakeholders	14	28	42	27
Founder of a state-owned or municipal enterprise	2	1	1	10
State Labour Inspectorate	4	12	8	7
Head of the administration of an enterprise	36	46	61	122
Liquidator of an enterprise	6	25	41	57
Banks	3	2	7	–
Ministry of Agriculture, head of district administration	–	7	1	2
Other creditors	6	18	48	97

**Table 5.** Assets and financial obligations of enterprises in bankruptcy and bankrupt enterprises according to activities as of December 31, 2001

Codes of classification of economic activities	Types of activity	Number of enterprises	Assets of enterprises, million LTL	Debts, million LTL	Property of enterprises compared with debts, per cent
	Total	1606	1852,59	5216,87	35,5
0–14	Agriculture, cattle-breeding, fishing, coal-mining	107	60,35	277,22	21,8
15–37	Manufacturing	562	1116,23	3075,41	36,3
40–42	Supply of electricity, gas, and water	4	0,92	4,21	21,9
45	Construction	169	119,80	420,36	28,5
50–52	Wholesale and retail trade	565	355,93	933,60	38,1
55	Hotels and restaurants	40	2,96	15,65	18,9
60–64	Transport, storage and communication	60	32,86	152,48	21,5
65–67	Financial intermediation	16	30,37	49,28	61,6
70–75	Real estate, renting and business activities	46	122,77	224,50	54,7
80	Education	1	–	0,03	–
85	Health and social work	4	0,17	4,60	3,7
90–93	Other community, social and personal service activities	33	10,23	59,53	17,2

a given enterprise. A relatively better state of affairs was in the companies operating in the sphere of other community, social and personal service, hotels and restaurants as well as transport, storage, and communication.

According to the data, financial obligations of enterprises in bankruptcy and bankrupt enterprises to banks and mortgage creditors have the largest comparative weight – 28,6 per cent. The debt of enterprises to the state budget makes up 23,1 per cent. Financial obligations of enterprises to other creditors (agricultural workers, energy companies, payment for goods, etc.) constitute 34,2 per cent. Debts of companies to the State Social Insurance Fund amounted to 10,0 per cent and to employees reached 4,1 per cent of the total sum of arrears.

A tendency is evident that the size of enterprises in bankruptcy is continuously decreasing. Each of 591 companies which in 2001 started bankruptcy procedures had on average 16,2 employees, while in 2000 in 414 such companies there worked on average 19,1 employees and over the entire period of 1993-2000 enterprises in bankruptcy employed on average 44,2 persons. The dynamics of changes in the number of employees of enterprises in bankruptcy is shown in Table 6 [10].

According to the number of employees, all the enterprises in bankruptcy can be divided in the following way: the companies employing more than 250 persons make up 2,7 per cent, the companies employing less than 250 persons account for 8,9 per cent, those with less than 50 employees make up 17,1 per cent, and those having less than 10 employees – 71,3 per cent.

A rapidly increasing number of enterprises in bankruptcy leads to detrimental economic and social consequences. One of them is growing unemployment. According to preliminary data, 1606 enterprises in

bankruptcy and bankrupt enterprises (over the period of 1993-2001) as of the day of announcing them bankrupt employed 58847 persons and until the end of 2001, 53498 employees were dismissed from these companies, which accounts for 90,9 per cent of all the persons working in them. The companies currently undergoing bankruptcy procedures (there were 1153 such companies on January 1, 2002) had 36551 employees at the beginning of the process, out of whom 27888 were dismissed until January 1, 2002. Only in 2001 6577 employees were dismissed in Lithuania, which twice as many as in 2000.

The analysis of the data related to the change in the number of employees of the enterprises in bankruptcy and bankrupt enterprises operating in different spheres of activity allows to conclude that the number of employees has rapidly decreased in the companies operating in the spheres of health and social work (by 99,1 per cent), hotels and restaurants (by 98,9 per cent), agriculture (by 93,4 per cent), and real estate, renting, and business activities (by 92,7 per cent). Changes in the number of employees of enterprises in bankruptcy and bankrupt enterprises according to activities over the period of 1993-2001 are presented in Table 7 [9].

The analysis of the economic and financial data of companies presented by the State Tax Inspectorate points out to a certain positive tendency, namely, decrease in the number of the enterprises that are experiencing economic difficulties and have already become insolvent or unprofitable. The analysis shows that out of 36689 companies which have submitted their financial accounts, 13347 enterprises are unprofitable and employ 259230 persons [9]. The number of such companies decreased from 42,3 per cent in 1999 to 36,4 per cent in 2000, including small and medium-size enterprises (having less than 50 employees), which made up 64,5 per cent in 1999 and 62,2 per cent in 2000. The number of unprofitable small and

**Table 6.** Division of enterprises in bankruptcy and bankrupt enterprises according to the number of employees

Year	Total	Less than 10 employees	10–49 employees	50–249 employees	250 and more employees
1993–2001	1606	1145	274	143	44
1993	6	2	0	2	2
1994	27	12	4	7	4
1995	36	8	9	8	11
1996	79	37	20	17	5
1997	108	57	26	22	3
1998	98	60	25	13	0
1999	247	180	37	26	4
2000	414	302	78	28	6
2001	591	487	75	20	9

medium-size businesses decreased from 27,3 per cent in 1999 to 22,6 per cent in 2000.

In 2000, there were 13907 insolvent companies whose liabilities were in excess of half of their assets (excluding the terms of the discharge of the obligations) and which employed 236494 persons. The number of such businesses decreased from 44,8 per cent in 1999 to 37,9 per cent in 2000.

The number of insolvent enterprises whose liabilities were in excess of the value of all the assets decreased from 16 per cent in 1999 to 14,5 per cent in 2000. The latter include small businesses with less than 10 employees, which made up 84,7 per cent in 1999 and 84,3 per cent in 2000. The number of these companies decreased from 13,5 per cent in 1999 to 12,3 per cent in 2000.

In 2001, research was conducted on the causes of the protraction of bankruptcy proceedings and the insolvency of enterprises. The data of the interviews of district court judges and the information collected from administrators have shown that the main reasons for protracting bankruptcy procedures are delayed

criminal proceedings instituted and appeals launched against the chief executives of enterprises or other persons, low demand for the assets of enterprises in bankruptcy or the fact that companies do not have sufficient assets even to defray administrative costs [10]. A considerable number of bankruptcy procedures are also protracted due to the activity of administrators.

The accumulated and analysed data on insolvent and unprofitable enterprises have shown that the main reasons for the insolvency and unprofitability of companies are as follows:

- little use made of the production capacities of enterprises;
- shortage of circulating capital;
- inefficient use of fuel, energy resources, local raw materials, and other material resources;
- inactivity of the management bodies of companies and reluctance to take timely measures to solve the problems of the reorganisation of a company, alteration of the size of its capital, liquidation of the company, etc.;

**Table 7.** Changes in the number of employees of enterprises in bankruptcy and bankrupt enterprises according to activities over 1993-2001

Codes of classification of economic activities	Types of activity	Number of enterprises	Number of employees			
			At the beginning of bankruptcy procedures	At the end of period under review	Number of employees dismissed	Number of employees dismissed, per cent
	Total	1606	58847	5349	53498	90,9
0–14	Agriculture, cattle-breeding, fishing, coal-mining	107	2791	184	2607	93,4
15–37	Manufacturing	562	44694	3739	40955	91,6
40–42	Electricity, gas and water supply	4	304	54	250	82,2
45	Construction	169	3178	515	2663	83,8
50–52	Wholesale and retail trade	565	4139	429	3710	89,6
55	Hotels and restaurants	40	527	6	521	98,9
60–64	Transport, storage and communication	60	854	235	619	72,5
65–67	Financial intermediation	16	197	31	166	84,3
70–75	Real estate, renting and business activities	46	1726	126	1600	92,7
80	Education	1	–	–	–	–
85	Health and social work	4	224	2	222	99,1
90–93	Other community, social and personal service activities	33	213	28	185	86,9

- inability of enterprises to adapt to market conditions and lack of aggression when looking for new markets;
- slow restructuring of large companies;
- insufficient control of the financial accounting of companies.

A rapidly growing number of bankrupt businesses and the necessity to timely institute bankruptcy proceedings and to speed bankruptcy procedures were one of the most important reasons for the preparation of a new edition of the Enterprise Bankruptcy Law.

Moreover, the fact that information about the companies which are experiencing difficulties and which frequently need only little assistance to improve their financial situation and to re-establish their competitiveness is ineffective and late by a year or even a year and a half as well as a large number of insolvent enterprises have made it necessary to pass the Law on Restructuring of Enterprises.

The new Enterprise Bankruptcy Law and Law on Restructuring of Enterprises together with supplementary legislation and the amendments of other related legal acts were adopted by the Sejm of the Republic of Lithuania and entered into force on July 1, 3 and 5, 2001. These legal acts enable enterprises to simplify and speed up bankruptcy procedures, in particular the procedure for selling the assets of enterprises in bankruptcy, and allow them to start dealing with their financial difficulties earlier.

The implementation of the Enterprise Bankruptcy Law and Law on Restructuring of Enterprises as well as related legislation creates conditions for improving of the quality of bankruptcy and restructuring procedures, financial discipline and competitiveness of enterprises, and for alleviating detrimental social and economic consequences of the bankruptcies of different companies. A positive improvement in the legal regulation of businesses in bankruptcy leaves the hope that the number of bankrupt companies will decrease. The creation of a bankruptcy prevention system would also contribute to averting bankruptcy and reducing its risk.

### 3. Conclusions

1. The problem of bankruptcy is a very sore issue for Lithuania. The major causes of the bankruptcy of companies are external factors: radically changing economic conditions, losing of old markets, changes in the form of ownership, etc. Internal factors are also significant, particularly the competence of the top management and the personnel as well as prepared-

ness to work in market conditions. However, it is also necessary to point out the positive role of the bankruptcy, which is related to a growing competition in the contemporary market economy and the acceleration of changes allowing the best companies alone to survive on the market.

2. Over the period of 1993-2002, 1606 enterprises and 14 banks were declared bankrupt. However, bankruptcy procedures have only been completed in 453 companies, out of which 424 companies have been liquidated, 4 reorganised, 9 sanated, and in the case of the remaining 16 bankruptcy proceedings have been suspended or composition with creditors has been reached. At the beginning of 2002, restructuring was in progress in 2 enterprises and 30 companies were preparing for this procedure.

3. These data show a firm tendency of the increase in the number of enterprises in bankruptcy by 1,4-1,7 times annually. This growth has been the most noticeable for the last 3 years.

4. The analysis of the duration of the bankruptcy process in enterprises in bankruptcy and bankrupt enterprises shows that there remain a considerable number of protracted bankruptcy procedures, which were started more than three years ago (over 1993-1998). At the end of 2001, the bankruptcy procedures that started in the period of 1993-1998 were still in progress in 147 companies. However, bankruptcy processes are accelerating thanks to the implementation of the new Enterprise Bankruptcy Law, which entered into force on July 1, 2001.

5. Over the period of 1993-2001, enterprises in bankruptcy and bankrupt enterprises were predominantly trading (35,1 per cent) and industrial (34,9 per cent) companies (Table 3) [9]. In total, these enterprises make up 70 per cent of all the enterprises in bankruptcy and bankrupt enterprises. The percentage of trading companies in bankruptcy as compared with all the enterprises in bankruptcy is steadily growing each year, whereas that of industrial companies is decreasing by several per cent.

6. A tendency is evident that the size of enterprises in bankruptcy is continuously decreasing. The enterprises in bankruptcy tend to have less than 10 employees or between 10 and 50 employees.

7. The generalisation of research data has enabled to establish a certain positive tendency, namely, decrease in the number of the enterprises that are experiencing economic difficulties and have already become insolvent or unprofitable.

8. A positive improvement in the legal basis of bankruptcy and restructuring leaves the hope that the number of bankrupt companies will decrease, although some problems remain unsolved. One of such problems is an insufficient bankruptcy prevention system, both at the micro and the macro level. A timely and comprehensive bankruptcy diagnostics as part of the bankruptcy prevention system could reduce the bankruptcy risk and in the majority of case help to avert bankruptcy.

## References

1. Roberts Mark.A. Lessons Learned in Bankruptcy, Air Conditioning Heating & Refrigeration News, 2004, Vol.221, Issue 10, p. 1–4.
2. Bankruptcy figures. Credit Management, 2004, p. 1–10.
3. Heiss Florian, Koke Jens. Dynamics in Ownership and Firm Survival: Evidence from Corporate Germany, European Financial Management, 2004, Vol.10, Issue 1, p. 167.
4. McGregor Sue, Klingander Birgitta, Lown Jean. Comparative Analysis of Canadian, American and Swedish Bankruptcy Policy: Why do Governments Legislate Consumer Debt? International Journal of Consumer Studies, 2001, Vol.25, Issue 3, p. 208.
5. Beddington Rob. The ICSA Insolvency Guide, Credit Management, 2004, p. 42.
6. Lietuvos Respublikos įmonių bankroto įstatymas. *Vals-tybės žinios*, 1992, Nr. 29–843.
7. Lietuvos Respublikos įmonių bankroto įstatymas. *Vals-tybės žinios*, 1997, Nr. 64–1500.
8. Lietuvos Respublikos įmonių bankroto įstatymas. *Vals-tybės žinios*, 2001, Nr. 31–1010.
9. Įmonių bankrotas 1993–2001 m. Vilnius: Statistikos departamentas prie Lietuvos Respublikos Vyriausybės, 2002.
10. Lietuvos ekonomikos apžvalga 2002 m. Nr. 1. Vilnius: Statistikos departamentas prie Lietuvos Respublikos Vyriausybės, 2002.