

*Organisation for Economic Co-operation and Development
the World Bank
Asia Pacific Economic Cooperation
and
the Australian Treasury
with the support of
AusAID*

**INSOLVENCY SYSTEMS IN ASIA: AN
EFFICIENCY PERSPECTIVE**

Final agenda

*Hotel Inter-Continental
Sydney, Australia
29-30 November 1999*

Monday 29 November 1999

08:30 – 08:45 **Registration**

08:45 – 09:15 **Opening session:**

Chairman: *Mr. Gary Potts*, Executive Director, Markets Group, The Treasury, Canberra

Opening address:

The Honourable Joe Hockey, Minister for Financial Services and Regulation, Canberra

Welcoming remarks:

Mr. William Witherell, Director, Directorate for Financial, Fiscal and Enterprise Affairs, OECD

Mr. Douglas Webb, Legal Adviser, Finance and Private Sector Development, The World Bank

09:15 – 10:45 **SESSION I**
Presentation of the draft World Bank Principles and Guidelines for Effective Insolvency Systems

Chairman: *Mr. Stilpon Nestor*, Head of Corporate Affairs Unit, Directorate for Financial, Fiscal and Enterprise Affairs, OECD

Presentations by: *Mr. Gordon W. Johnson*, Senior Counsel, Legal Department, The World Bank
Mr. Koji Takeuchi, Partner, Sakura Kyodo Law Offices, Tokyo

General discussion

10:45 – 11:00 *Coffee break*

11:00 – 12:45 **SESSION II**
Asian insolvency regimes from a comparative perspective: Problems and issues for reform

Chairman: *Mr. Lawrence S. Liu*, Partner, Lee and Li, Taipei

Presentations by: *Dr. Il Chong Nam*, Korea Development Institute, Seoul

Discussants: *Mr. Kishore Soni*, Chief Executive, Soni Industrial Restructuring Consultants (SIRCON), New Delhi
Prof. Roman Tomasic, Dean, Faculty of Business and Law, Victoria University, Melbourne
Prof. Wang Weiguo, Dean, Department of Economic Law, China University of Politics and Law, Beijing

General discussion

12:45 – 14:00 *Lunch*

14:00 – 16:00 **SESSION III**
Workouts and restructurings

- The London Approach and its offspring
- The interface with formal proceedings
- Exit mechanisms
- The insolvency test

Chairman: *Mr. Timothy B. DeSieno*, Partner, Bingham Dana LLP, Singapore

Panel discussion: *Mr. Jusuf Anwar*, Chairman, Capital Market Supervisory Agency, Jakarta
Ms. Kanjana Chanyarungrojin, Assistant Secretary-General, Financial Sector Restructuring Authority, Bangkok
Datuk C. Rajandram, Chairman, Corporate Debt Restructuring Committee, Kuala Lumpur

General discussion

16:00 – 16:15 *Coffee break*

16:15 – 18:00 **SESSION IV**
Sustaining firm operations

- Creditor or debtor control
- Financing continued operations
- Facilitating rescue through procedural design
(unitary vs. multi-track proceedings)

Chairman: *Mr. Neil Cooper*, President, International Federation of Insolvency Practitioners

Panel discussion: *Dr. Manfred Balz*, General Counsel, Deutsche Telekom AG, Bonn
Mr. Tim Cumming, Partner, PricewaterhouseCoopers, Sydney
Mr. John Lees, Partner, Ferrier Hodgson, Hong Kong

General discussion

19:30 ***Official Dinner***
Keynote speaker: *Mr. John Lockhart*, Executive Director, Asian Development Bank

Tuesday 30 November 1999

8:45 – 10:15

SESSION V

Creditor rights

- Absolute priority
- Administrative and tax claims
- Stakeholder claims
- Debt for equity swaps
- Secured creditors
- Treatment of foreign creditors

Chairman:

Mr. Douglas Webb, Legal Adviser, Finance and Private Sector Development, The World Bank

Panel discussion:

Prof. Soogeun Oh, College of Law, Inha University, Incheon
Mr. Salman Ali Shaikh, Senior Executive Vice President, Habib Bank, Karachi
Mr. Lampros Vassiliou, Allens Arthur Robinson Group, Bangkok

General discussion

10:15 – 10:30

Coffee break

10:30 – 12:00

SESSION VI

Systemic distress

- Linkages between financial and corporate distress
- Markets for distressed assets
- Insolvency and small and medium sized businesses

Chairman:

Ms. Veronique Ingram, General Manager, Corporate Governance and Accounting Policy Division, The Treasury, Canberra

Panel discussion:

Mr. John R. Knight, Chief Regional Counsel for Southeast Asia and India, The Chase Manhattan Bank, Singapore
Mr. Rabindra S. Nathan, Partner, Shearn Delamore & Co, Kuala Lumpur
Mr. Jechul Yoon, General Manager, Treasury and Accounting Department, Korea Asset Management Corporation (KAMCO), Seoul

General discussion

12:00 – 13:30

Lunch

13:30 – 15:00 Session VII
Insolvency institutions: courts, state agencies and practitioners

- The skills crisis
- Cross border issues

Chairman: *Mr. Philip Crutchfield*, Victorian Bar, Melbourne

Panel discussion: *Mr. Danilo Concepcion*, Commissioner, Securities and Exchange Commission, Manila
The Hon. Chiyong Rim, Research Judge, Supreme Court of Korea, Seoul
Mr. Terry Taylor, Partner, Ferrier Hodgson, Sydney
The Hon. Wisit Wisitsora-at, Executive Director, Business Reorganisation Office, Legal Execution Department, Bangkok

General discussion

15:00 – 15:15 *Coffee break*

15:15 – 16:45 Concluding discussion

- Reflections on global principles (World Bank)
- The way forward (World Bank, OECD, APEC, INSOL)

Chairman: *Mr. William Witherell*, Director, Directorate for Financial, Fiscal and Enterprise Affairs, OECD

Discussants: *Mr. Douglas Webb*, Legal Adviser, Finance and Private Sector Development, The World Bank
Mr. Stilpon Nestor, Head of Corporate Affairs Unit, Directorate for Financial, Fiscal and Enterprise Affairs, OECD
Mr. Terry O'Brien, APEC Special Adviser, The Treasury, Canberra
Mr. Neil Cooper, President, International Federation of Insolvency Practitioners

Concluding discussion

Notes to the Agenda

1. The meeting will start at 8:45 on 29 November and finish at 16:45 on 30 November. The main presentations should be limited to approximately 15-20 minutes and discussants should try to limit their comments to 5-10 minutes. These relatively stringent time limits are required in order to have ample time for general discussion.

2. In addition to the presentations, there will be background country reports available for Korea (an OECD Member country), India, Indonesia, Malaysia, the Philippines, Singapore, and Thailand. Each country report contains a discussion of the following issues: the extent to which the surveyed country was affected by the recent Asian economic crisis; the characteristics of debtor-creditor relationships in that country; formal and informal insolvency mechanisms and procedures; efficiency of insolvency mechanisms and procedures; and problems and areas in need of reform.

3. The principal objectives of the meeting are:

- To bring together senior policy makers and members of the judiciary responsible for insolvency reform and its implementation, private sector practitioners (including representatives of the financial sector) and experts from the Asian region with senior OECD Member country experts (both from the policy side and the private sector) to exchange experience on the design of insolvency laws and procedures, review progress in insolvency reform, and offer recommendations for the future;
- To present and discuss the draft World Bank Principles and Guidelines for Effective Insolvency Systems; and
- To discuss possibilities for follow-up work and the monitoring of progress.

4. *Session I* will focus on highlights of The World Bank's Insolvency Initiative and its emerging principles and guidelines for building effective insolvency systems, which addresses legal, institutional and regulatory frameworks, business and financial sector concerns and related debtor-creditor rights issues, the design of rehabilitation models and alternative insolvency models, and a variety of specialised phenomena, such as systemic crises, dealing with state-owned enterprises, and bank insolvencies.

The Initiative is an outgrowth of the wider effort to improve the future stability of the international financial system and aims to identify principles and guidelines for sound insolvency systems and for the strengthening of related debtor-creditor rights in emerging markets. The initiative was commenced in the wake of the East Asia financial crisis, the aftershocks of which continue to be felt among the domestic banks and companies of the region. The initiative is a genuinely international endeavour, undertaken in partnership with the International Monetary Fund, International Finance Corporation, all of the Regional Development Banks, the OECD, UNCITRAL and the leading international insolvency associations, INSOL and IBA (Committee J).

With tightening credit markets and companies struggling to survive, the challenge today is to breathe new life into bankruptcy systems to promote restructuring of viable businesses and efficient closure and transfer of assets for failed businesses. Recognising the complexity of economies, and the diversity in legal systems and their unique cultural expressions, the Initiative does not envision the creation of a one-size-fits-all model. Rather, the Initiative aims to develop a diagnostic tool for self-assessment, which takes into account important and relevant variables that should be considered in designing an appropriate insolvency system, with a proper respect for global economics and current insolvency trends. An effective system will embrace specific policy choices that balance the strengths and weaknesses of different facets of the broader system.

Main issues for discussion:

What are the fundamental functions, features and design considerations of an insolvency system?

What is the role and significance of the judiciary and regulatory bodies, and how does system design take into account issues of capacity?

How design features balance competing policies and interests (e.g., creditors, debtors, employees, government, etc.). Do specialised cases (financial institutions, insurance companies, state-owned enterprises) and unique circumstances (systemic crises) require special insolvency procedures or should these be addressed in a single insolvency regime?

How can the World Bank principles and guidelines for effective insolvency systems be utilised by Asian countries in their reform efforts?

5. In **Session II**, the discussion will focus on a set of comparative conclusions drawn from the OECD insolvency reviews of Asian economies. The presenters will analyse the general role and evolution of insolvency systems in Asia prior to, during, and after the recent economic crisis. They will also review current reform efforts in the region and identify problem areas that need to be addressed.

Main issues for discussion:

How have the insolvency regimes in Asia fared under the recent economic crisis?

What are the main problems with the current insolvency mechanisms in Asia in terms of efficiency and fairness? What has been the progress and content of efforts to remedy weaknesses that have surfaced?

What are the major reform efforts that have been undertaken in recent years? What has been the progress?

6. **Session III** will analyse informal (workouts) and formal insolvency procedures as applied in the Asian context, although useful insights gained from the experience of certain OECD countries will also be shared.

In many countries, particularly those where the insolvency laws and mechanics are poorly developed, informal procedures are of equal, if not greater, importance than formal procedures. Even in countries with well-developed insolvency regimes, many debtors and creditors prefer to use informal proceedings because of their speed, flexibility, and reduced costs. The rapidity in which informal procedures can be deployed is particularly significant, as speed is critical when a company is teetering on the edge of bankruptcy. Given these advantages, a number of countries have formulated guidelines to encourage the use of informal insolvency mechanisms. The most successful among these are the London Approach guidelines, promulgated by the Bank of England to encourage banks to use workouts rather than subjecting companies to the formal insolvency process.

In response to recent economic difficulties, certain Asian governments have also formulated their own guidelines, such as the Jakarta Initiative in Indonesia. In Thailand, leading domestic banks have adopted a Framework for Corporate Debt Restructuring in Thailand, which aims to encourage the use of procedures outside of the formal bankruptcy process. Korea, an OECD Member country, has adopted a variant of the London Approach as well.

While informal proceedings can be a speedy and effective way of dealing with insolvency, one should not underestimate the importance of an effective formal insolvency regime. In the rehabilitation setting, a well-functioning formal insolvency system is crucial because it provides parties engaged in an informal workout with a powerful incentive to conclude an agreement. When it is not possible to return a company to profitability through a workout, formal bankruptcy procedures offer the optimal means for a firm to exit the market in an orderly fashion. In situations where multiple creditors have provided financing to a company, the absence of formal procedures will often lead to a “grab race” whereby the first creditors to seize the assets of the distressed firm will have their claims satisfy in full while creditors who are latecomers end up with nothing. In most cases, the grab race will also obliterate the firm’s going concern value. Furthermore, if an effective formal insolvency regime is lacking, informal approaches risk generating strategic behaviour by creditors and, especially, debtors.

Finally, the greatest weakness of informal arrangements is that there are no clear formal requirements in which they can be anchored.

Main issues for discussion:

Assess the advantages and disadvantages of informal insolvency procedures. Have efforts to use informal procedures in Asia been effective?

Discuss the interplay between formal and informal procedures. In the context of Asia, how can informal procedures complement formal mechanisms?

How should insolvency be determined (balance sheet test or cessation of payments test)? Discuss the advantages and disadvantages of each approach, particularly its impact on efficiency and fairness for all parties involved.

Who should be granted the right to initiate an insolvency proceeding (debtor, creditor, government)? What requirements should be imposed on those seeking to initiate an insolvency proceeding? Should the threshold requirements differ for the debtor, creditors, and the government?

Discuss the importance of speed in the process of declaring bankruptcy. How can concerns in this area be addressed in practice?

7. In **Session IV**, the discussion will centre on the means utilised to sustain the operations of an insolvent company in order to maximise its value. In an increasing number of countries, the initiation of formal insolvency proceedings results in the imposition of a moratorium on the enforcement of creditors' rights. In these countries, such a moratorium is considered essential to effectuate an orderly liquidation or to provide the distressed firm with breathing space to recover from its financial difficulties. While extending the moratorium to secured creditors might be a prerequisite for its effectiveness, it might also create tensions because such treatment frustrates the basic aim of security interests to protect the creditor in the event the debtor becomes insolvent and also reduces the predictability of contractual relations. These tensions must be adequately addressed.

A critical matter to be decided at the outset of an insolvency proceeding is whether current management is to retain a continuing role in the firm. This issue is particularly important when rehabilitation is to be attempted. The suitability of current management to continue running the insolvent enterprise is often questioned because these managers have brought the company to the brink of collapse. On the other hand, these same individuals also possess the best understanding of the business.

In all insolvency proceedings, creditors should be given the opportunity to play an active role to assist with the formulation of the reorganisation plan, in the case of a rehabilitation, and to otherwise monitor the debtor in possession or liquidator/administrator to ensure that the value of the enterprise is being maximised.

It is sometimes unclear at the commencement of the insolvency proceeding whether a firm should be rehabilitated or liquidated. It is therefore crucial that the insolvency law is sufficiently flexible so that creative and novel solutions can be found that will maximise the value of the firm (or its assets) for the sake of the creditors and society as a whole. In recent years, there has been a debate as to whether unitary proceedings serve this purpose better than separate tracks for liquidation, composition, and debtor-led reorganisation.

Main issues for discussion:

Assess the merits of imposing a moratorium on the enforcement of creditors' rights upon the initiation of an insolvency proceeding. To what extent should the moratorium be extended to secured creditors? What measures should be undertaken to protect the value of secured assets during the moratorium?

Should the debtor remain in possession of the insolvent enterprise? If so, what controls should be imposed to ensure that the value of the firm will not be further diminished? What powers should be granted to the liquidator/administrator, the court and creditors to supervise the debtor in possession?

How do you enhance value for the estate while minimising transaction costs? Which type of procedure, unitary, multi-track or a hybrid approach, is most efficient and cost effective? Can additional tools, such as non-cash bids, be employed to enhance value?

How important is the monitoring role of creditors in maximising the value of the firm?

8. **Session V** will analyse the rights and roles of creditors under insolvency law. One of the main principles of insolvency law is to treat similarly situated creditors equally. This, however, does not mean that all creditors should receive equal apportionment. To the extent that creditors have struck different bargains with the debtor, it may be more equitable and efficient for the insolvency law to recognise such differences when proceeds are distributed. On the other hand, it is important that the powerful position of certain creditors should not undermine solutions that enhance the value of the firm, thereby increasing social welfare.

While granting priority to the claims of secured creditors is consistent with insolvency law principles, a more controversial issue regards the preferences given to certain privileged claimants such as employees and tax authorities. In many cases, these preferences arose from political and social concerns rather than from a desire to achieve an efficient outcome. It may therefore be more appropriate to address many of these issues directly rather than through the insolvency law.

Although the absolute priority rule helps to preserve the integrity of the credit system, rigid adherence to this rule may lead to a less than optimal outcome. In situations where current shareholders-managers are to retain a degree of control of the distressed enterprise, it is important to implement incentives that will help align the interests of these individuals with those of the creditors. Such incentives may include allowing the shareholders-managers to retain an equity stake in the company even when current creditors have not been paid in full.

In order to enhance the prospects for long-term success, it is important that the insolvency law allows for a variety of arrangements to be proposed in a rehabilitation proceeding, including debt forgiveness, debt for equity swaps, and non-cash bids. In addition, foreign creditors and shareholders should be allowed to participate fully in these proceedings. In certain countries, this may require removing restrictions on foreign ownership of a domestic enterprise.

Main issues for discussion:

Should the absolute priority rule be applied in all cases? How widely is this rule recognised in Asian countries?

What are the primary means employed to protect the rights of creditors? How are secured creditors treated under the insolvency law?

What are some of the political and social concerns that must be taken into account when designing an insolvency system? How do you balance these concerns with the desire to ensure predictability? Can these concerns be addressed outside of the insolvency law?

Discuss the duty of directors to act in the best interest of shareholders. For a company facing financial difficulties, at what point should this duty shift from the shareholders to creditors?

Discuss the treatment of foreign claimants under the insolvency law and in recent Asian insolvency proceedings. What obstacles, if any, did foreign claimants encounter and how were such obstacles ultimately resolved?

9. In **Session VI**, the panelists will discuss issues relating to the systemic distress that recently struck certain Asian countries. Systemic distress, where major segments of the economy are on the verge of collapse due to severely deteriorated macro-economic conditions, must be distinguished from isolated cases of bankruptcies. Most insolvency systems, which are designed to handle individual

cases of insolvency, will not work properly in the context of systemic distress. Consequently, additional mechanisms must be developed to cope with systemic distress.

One approach could be active encouragement of voluntary out-of-court procedures. Another possible solution is to enact crisis-specific legislation to be applied in such systemic distress circumstances. Under such legislation, firms can be given a framework for restructuring their financial obligations. Because the increased protection provided to debtors under such legislation might invite strategic behaviour, it is imperative that any such legislation establishes clear rules outlining when such protection may be invoked and when it will be terminated.

Systemic distress will often result in the creation of specific institutions to deal with accumulating bad debts in the financial sector. These institutions might play a crucial role in addressing some of the systemic corporate insolvency issues. Another impact that these institutions might have is the encouragement of markets for distressed assets, which in turn could play an important role in rapidly reallocating resources in the economy.

Systemic distress will often impact disproportionately on smaller firms as they are more vulnerable to a sharp deterioration in the general macro-economic environment and the health of a few large suppliers/customers. In such situations, many countries envisage specific assistance measures to bring about an orderly reorganisation of small and medium-sized enterprises (SMEs).

Main issues for discussion:

During periods of systemic distress, where a high percentage of firms are technically insolvent, should there be a presumption toward rehabilitation rather than liquidation? What other crisis-specific protections should be provided?

What is the role of special institutions in the process of corporate reorganisation under conditions of systemic distress? Assess their effectiveness in the Asian context.

How can markets for distressed assets be developed?

What are the unique problems faced by small and medium-sized enterprises during periods of systemic distress? What measures can be undertaken to provide assistance to these enterprises?

10. **Session VII** will examine the institutional infrastructure required for an effective and efficient insolvency system. In many emerging markets, such infrastructure requires further development. Problems plaguing insolvency regimes in the Asian region include a dearth of qualified judges and other professionals, inadequate equipment and physical facilities, lack of funding for relevant state agencies, and corruption. In certain Asian countries, the neglect in this area can be attributed to decades of rapid economic growth, when governments saw little need to strengthen insolvency regimes and individuals had few opportunities or incentives to become insolvency specialists.

Building an effective infrastructure is a gradual, long-term process. The challenges facing governments are particularly formidable in this area because the complexity of insolvency law requires a critical mass of judges and other professionals such as lawyers, accountants, and administrators/liquidators who understand both the law and business and accounting concepts. Consequently, enacting strong legislation is only the first step in creating a well-functioning insolvency regime. In addition, nascent institutions must be nurtured and bankruptcy professionals must be trained. To rapidly develop the requisite capacity for a fully functioning insolvency regime, it may be desirable to create bankruptcy courts or specialised state institutions that focus exclusively on insolvency matters.

When reforming an insolvency system, a crucial issue to resolve is whether the insolvency law should adopt a “bright-line” approach that leaves judges and other relevant government officials with little discretion in applying the law or, alternatively, to endow these officials with considerable decision-making power. When corruption is rife or when there is a dearth of personnel capable of making sound legal and commercial decisions, the bright-line approach may appear to be an attractive solution. On the other hand, as each insolvency case is unique, it may not be possible for the insolvency law to invoke a set of rigid formulas that is applicable in all proceedings.

Main issues for discussion:

In terms of institutional infrastructure, what are the major problems facing the insolvency regimes in Asia? How can these shortcomings be overcome?

What measures can be undertaken in the short to medium-term to compensate for weak institutional capacity? Are there any models that have proven effective?

How much discretion should be given to judges and other government officials in applying the insolvency law?

Given the complex nature of insolvency law, is it necessary to create specialised bankruptcy courts? What alternatives exist when the lack of financial and other resources prohibits the creation of such courts?

11. In the ***Concluding Discussion***, the organisers will draw certain conclusions and explore the possibilities for future work and dialogue in the area of insolvency in order to sustain reforms and promote the emergence of effective insolvency systems in the region. Participants are also invited to provide their input in this important, forward-looking debate.