

BUSINESS INSOLVENCY IN THAILAND: REFORM AND REHABILITATION

Richard F. Broude
Law Offices of Richard F. Broude
New York City

INTRODUCTION

This report was commissioned by the OECD to provide an independent expert background and basis for a peer discussion of the Thai insolvency regime, in the context of the second meeting of the Forum for Asian Insolvency Reform (FAIR). While the opinions expressed here do not necessarily represent the OECD or other FAIR partners, the report has been edited to reflect a balanced view of key Thai issues and reform effort, and provide a preliminary set of recommendations for the future.

The report deals, in general terms, with bankruptcy and insolvency as a defining characteristic of a market economy; [one that] demarcates the limits of extending credit, confronting risk, entrepreneurial venture, and corporate self-determination; it engages all sectors of the economy; and it expresses fundamental conflicts at the heart of the capitalist political economy between labor and capital, owners and managers, debtors and creditors, and the state and the market.¹ The manner in which a particular country deals with a failing or distressed enterprise says volumes about the value that country places upon the bankruptcy goals of preserving value, saving jobs, and allocating resources.

In particular terms, this report addresses the manner in which Thailand's insolvency regime, formal and informal, has responded to the financial crisis that began in 1997 and affected most of the economies in Asia. It measures that system against the general goals set out above.

¹ Bruce G. Carruthers and Terence C. Halliday, *Rescuing Business*, 1 (Clarendon Press 1998).

Given the importance of bankruptcy regimes to a country's economy, it comes as no surprise that much has been written about how the various countries in the region responded to the crises, with a particular emphasis upon insolvency regimes.²

During the course of my investigations for this report, I was privileged to have met and spoken to many individuals in the public and private sectors who are intimately involved with seeing that Thailand deals in the best way possible with the fallout from the financial crisis. None of these individuals are identified by name in this report, and the conclusions that are drawn from these conversations are a synthesis of many views.

The focus here is upon rehabilitation, not liquidation, although Thai law provides for both. Until 1998, Thai insolvency law dealt solely with liquidation; rehabilitation was not provided for. As shall be seen, governmental agencies, along with the business and financial communities, invented informal procedures for dealing with the dislocations and failures caused by the 1997 crisis, and the legislature was not far behind. After amending Thailand's insolvency law in 1998 to provide for rehabilitation, the legislature again amended the law in 1999. However, the current status of Thailand's insolvency regime cannot be understood without a discussion of the events and processes that went before.

PART I: AN OVERVIEW OF INSOLVENCY REFORM: SETTING THE STAGE

A. Dealing with the Crisis.

The financial crisis that began in 1997 resulted in a number of extraordinary measures designed to stabilize Thailand's economy. Led by the International Monetary Fund (IMF), a

² See especially *Insolvency Systems in Asia: An Efficiency Perspective* (OECD 2001) (hereinafter *Insolvency Systems*).

number of institutions and governments agreed upon a loan program accompanied by prescribed reforms in a number of sectors of the Thai economy. The rescue package consisted of a 34-month standby arrangement value at US\$ 3.9 billion.³ The current Thai government is considering repayment of the IMF loan.

As events unfolded, the Government of Thailand realized that other measures were needed to deal with the dislocations caused by the trauma to economic activity. Thus, a nonintrusive market-led strategy for debt restructuring, *Brink* at 47, was adopted, that included tax relief, changes to the laws dealing with foreign investment and ownership of real estate, out-of-court mechanisms for workouts, and improvements in the country's bankruptcy, foreclosure, and secured-lending laws. *Id.*

Other reforms were instituted. These included establishment of the Thailand Financial Accounting Standards Board, strengthening the Institute of Certified Accountants and Auditors of Thailand, modernizing the rules governing listing on the Stock Exchange of Thailand, attempting to modernize disclosure requirements, revising the guidelines for corporate directors, and making financial reports more transparent, among other things.

B. Stating the Problem.

³ Ijaz Nabi and Jayasankar Shivakumar, *Back From the Brink*, 24-27 (World Bank 2001) (hereinafter *Brink*). The rescue package was accompanied by financial sector restructuring, fiscal policy, and monetary and exchange rate policy. *Brink* at 27.

In his recent and controversial book, *Globalization and Its Discontents*, by Joseph E. Stiglitz (hereinafter *Discontents*), Nobel price-winning economist, one-time Chairman of President Clinton's Council of Economic Advisers, and formerly the chief economist of the World Bank, the author observes, at 53, that "[f]iscal austerity, privatization, and market liberalization were the three pillars of Washington Consensus advice throughout the 1980s and 1990s. Professor Stiglitz argues that, while the Consensus may work in some countries, it is not a universal panacea for, and indeed may cause harm to, others.

Any analysis of the efficacy of informal and formal insolvency procedures must start with the setting in which these procedures are supposed to operate. And no one has set the stage any better than Judge Wisit who, after pointing out that the immediate effects of the Asian economic crisis were the flotation of the Thai baht and the consequent effect on companies that had borrowed in foreign currencies, high interest rates aimed at currency stabilization, currency outflow, and the shuttering of 56 finance companies affecting a large group of borrowers, states:

As in many other countries in Asia the lending practice in Thailand concentrated more on collateral rather than on an analysis of cash flows. More often than not, Thai banks and finance companies in their lending required personal guarantees from owners and directors of the borrowing entities. One of the reasons this condition was accepted by the debtors might be the precedent that personal guarantees were not normally called upon for settlement of debt. Another reason might be the difficulty in differentiating the interests of the directors and owners of the borrowing companies who were often the same persons or a closely related group of persons. Another weakness in the lending practice in Thailand was the emphasis on personal relationship.⁴

These conditions are exacerbated by the fact that Thailand, in common with other countries in the region, had weak and inefficient corporate governance structures in both corporations and financial institutions as well as ineffective prudential supervision. In addition, private banks (as well as non-bank financial companies) were owned and controlled by the same families that controlled the conglomerates. The result of these conditions is that large loans were frequently made by banks to companies controlled by the same families without much attention

⁴ Wisit Wisitsora-At, *Country Report for Thailand*, appearing in *Insolvency Systems*, *supra* n. 1, 397, 397-398.

paid to underwriting standards.⁵

The financial crisis resulted in business, accounting, and legal problems seldom if ever encountered before in Thailand. This circumstance led, in turn, to the hurried development of an informal way of dealing with financially distressed businesses and to the passage, in 1998 and 1999, of significant amendments to the Thai insolvency statute, which dated from 1940. Before the 1998 amendment, that statute had provided only for liquidation; the 1998 amendments for the first time provided a method of rehabilitating financially distressed enterprises. The 1999 amendments were designed to cure some of the perceived weaknesses of the 1998 statute. A separate piece of legislation, also passed in 1999, created the Central Bankruptcy Court.

C. The Role of International Organizations in Insolvency Reform.

In some not insignificant part, the legislative developments (as well as other policies adopted by the Thai government) were part of the rescue package described above. Many of the international institutions that participated in the rescues of countries in distress, led by the World Bank and the IMF, insisted that any financial aid designed to ease the effects of the crisis be accompanied by legislative modernization, with a focus upon insolvency laws.⁶

The so-called World Bank Insolvency Initiative resulted in a paper entitled *Principles*

⁵ Il Chong Nam & Soogeun Oh, *Asian Insolvency Regimes from a Comparative Perspective: Problems and Issues for Reform*, appearing in *Insolvency Systems*, *supra* n.2, 19, 33-35.

⁶ *Discontents*, *supra* n. 3 at 118, argues that the IMF strategy for corporate restructuring was flawed because it led debtors to believe that real restructuring could be delayed, if not put off forever, by foot-dragging and other tactics of delay. In addition, the author states, at p. 18, that after the 1997 Asian crisis, IMF policies exacerbated the crises in Indonesia and Thailand.

*and Guidelines for Effective Insolvency and Creditor Systems.*⁷ In 1999, the IMF published *Orderly & Effective Insolvency Procedures: Key Issues*. The Asian Development Bank, in its 1999 and 2000 annual reports, detailed at length its Regional Technical Assistance for Insolvency Law Reform project, or RETA. The ADB's 1999 report, entitled *Insolvency Law Reform in the Asian and Pacific Region* in *Law and Development at the Asian Development Bank*, 1999 Edition, pointed to many of the inadequacies of the legal regimes in the region, and in particular, the failings of the insolvency regimes in the Bank's developing member countries in Asia. *Id.* at 7.

Each of these organizations called for the enactment of modern insolvency legislation, for improvement in the judicial systems employed to enforce that legislation, and for transparency. Suggestions were proffered as to how these admirable goals might be attained.

D. The Key Areas of Insolvency Reform.

At a November, 1999, meeting in Sydney, Australia, sponsored by the OECD and others, entitled *Insolvency Systems in Asia: An Efficiency Perspective*, certain conclusions were reached about the importance of insolvency reform. As reported in *Insolvency Systems* at 8-16, these conclusions were:

- *□ An efficient and effective insolvency system is pivotal for long-term economic recovery and growth.
- *□ There is no one-size fits all solution.
- *□ Notwithstanding the considerable flexibility in designing a well-functioning

⁷ The principles and guidelines are set out in Gordon W. Johnson, *The World Bank's global insolvency principles*, appearing in *Global Insolvency & Restructuring Review* 28 (May/June 2001).

insolvency system, certain core features are essential to all insolvency regimes.

Included within this rubric are efficiency, predictability, the realization that not all businesses can be saved some must be liquidated, an appropriate balancing of debtor and creditor rights, and dealing with shortcomings in the institutional infrastructure.

- * Formal and informal mechanisms should complement and support one another.
- * Insolvency reform must be accompanied by a broader set of reforms in related areas.

Focusing more specifically on statutory reform, a specific set of criteria were used in FAIR I by which one should judge the efficacy of a rescue statute. These are:

- * **Access.** Does the law enable the reorganisation process to be easily and inexpensively commenced?
- * **Automatic stay.** Does the law provide for an immediate automatic stay?
- * **Continued Management.** Does the law adequately provide for the ongoing management and control of an enterprise that seeks to be reorganised?
- * **Provision of new money.** Does the law provide for a commercially sound form of priority for the on-going finance funding that may be required to keep the enterprise liquid?
- * **Time frame.** Does the law provide for a speedy but sensible time frame for the progress of a case of reorganisation?
- * **Information to creditors.** Does the law adequately provide for creditors to receive sufficient and reliable information concerning the enterprise and the reorganisation proposal or plan?
- * **Voting rights and requirements.** Does the law adequately provide for creditor voting rights and their exercise?
- * **Basic requirements of reorganization plans.** Does the law ensure that a plan

of reorganisation meets some fundamental basic requirements?

- * □ **Supervision of the process.** Does the law provide for adequate overall supervision of the reorganisation process?
- * □ **Conversion to liquidation.** Does the law provide for conversion to liquidation if creditors do not accept a reorganisation plan or if the plan is not implemented? ⁸

There can be no quarrel with the proposition that these criteria are among the hallmarks of sophisticated and workable insolvency regimes. Whether enactment of a sophisticated insolvency statute leads to a sophisticated insolvency system is, however, a different matter altogether. One must remember always, as Professor Stiglitz points out, that one cannot simply graft the laws of one country onto the customs and norms of another. *Discontents*, p. 237. After all, it took the United States the better part of a century, which included the Great Depression and two world wars, to arrive at present chapter 11, one of the sources of the 1998 Thai legislation. Some things, it can safely be concluded, don't happen overnight. As has been stated:

[W]hat is required, perhaps more urgently in Thailand than elsewhere, is an understanding of closely controlled companies. Even though they may be listed on the Stock Exchange of Thailand, a number of these organisations have what could euphemistically be termed a unique approach to financial control, corporate governance and indeed, their trading practices. ⁹

⁸ These criteria were proposed to FAIR I by Clare Wee & Ron Harmer, *Insolvency Reform in Asia: An Assessment of Recent Developments and the Role of the Judiciary*, pp. 6-7, 11, presented at the Forum For Asian Insolvency Reform, Bali, Indonesia, February 2001. The authors go on to address other areas of concern, such as the development of an effective and honest judiciary with adequate resources to do the job assigned it, as well as the development of enough qualified people to perform as management of reorganizing debtors.

⁹ Steven Miller, *Corporate restructuring and insolvency: the view from Thailand*, appearing in *Global Insolvency and Restructuring Review*, page 15 (June/July 2000).

An assessment of the efficacy of the Thai system need not and should not contain invidious comparisons to the administration of insolvency systems in other countries, particularly those that have had decades to develop out-of-court mechanisms, insolvency legislation, and a sophisticated, honest, and well-paid corps of judges, trustees, and other administrators to manage the system created by the legislature and the participants in the credit industry. It should be made in light of the Thai culture and legal system, and address the manner in which the Thai insolvency system, including the amendatory legislation, has addressed Thai needs in light of that culture and that legal system.

PART II. THE THAI INSOLVENCY SYSTEM AND ITS IMPLEMENTATION

AFTER THE ASIAN CRISIS

A. The Legislative Framework.

The 1997 crisis led to reforms in both the informal and formal insolvency systems. First, the Financial Sector Restructuring Authority (FRA) was established to take over the operations of 58 finance companies that were suspended following the crisis. All but two were closed, and the FRA held auctions to dispose of the assets of the finance companies. However, complex profit sharing arrangements entered into to maximize sales prices has led to difficulties in computing dividends to creditors.

Next, the 1998 and 1999 amendments to the Thai laws for the first time provided for a rehabilitation regime. The legislation has been described as a hybrid of US chapter 11 reorganization and the Judicial Management of the Singaporean law.¹⁰ When the 1998 legislation was found to have some gaps and deficiencies, the 1999 legislation was passed in an attempt to cure them.

The reforms encompassed by the legislation can be evaluated for present purposes by returning to the criteria developed at Fair I.

- *□ **Access.** One of the most problematic areas of the Thai law is its insistence that the rehabilitation procedure be available only to businesses that are insolvent using the balance sheet test (assets are less than liabilities).¹¹ Mandating balance-

¹⁰ Wisit, *supra* n. 4 at 404.

¹¹ Other criteria are that the debtor owes at least THB 10 million and that there exist reasonable grounds and means to reorganize the debtor s business operations.

sheet insolvency as the prerequisite to qualifying for rehabilitation means, among other things, that unless out-of-court procedures are in place and work, by the time a company qualifies for rehabilitation it may be too late. Long delays are the usual result when an involuntary petition is filed and the debtor contests solvency. Objective standards of proof are more readily available to show failure to pay debts as they come due than to demonstrate asset valuation or discover and evaluate off-balance sheet debt. At the present time, studies are underway regarding the possible amendment of the financial standard for commencing a proceeding. It may be that the standard should be different for voluntary and involuntary petitions.

* □ **Automatic stay.** An immediate and broadly applicable stay of creditor secured and unsecured proceedings comes into effect upon the court's acceptance of the reorganization petition. Acceptance generally is obtained the day after the petition is filed. The stay may be modified if, *inter alia*, a creditor is not being adequately protected. The stay also prevents the initiation or continuation of a petition seeking bankruptcy. The stay remains in effect until the time for implementation of the plan expires, or the plan has been successfully implemented, or when the court takes certain actions, such as dismissing the petition.

* □ **Management of the Debtor.** If the petition is approved by the court, a reorganization order will be issued and a planner appointed. The planner controls the assets and business of the debtor, and also succeeds to shareholders rights (except for the right to receive dividends). The planner must prepare a

reorganization plan within three months (subject to two one-month extensions) of being notified of his/her appointment. Because of the possibility of personal liability under certain circumstances, the Planner tends to be a specially incorporated vehicle consisting of the debtor's existing management, or an accounting firm, or a joint venture between management and such a firm.¹² The difficulties of such a regime were pointed out by Wee & Harmer, *supra*, when they observed that suspending management power in favour of an independently appointed manager . . . has created some tension in Thailand because of a strong cultural aversion, mainly from owners and managers of corporations, to surrendering complete control. It seems not uncommon for the planner to be suggested by the debtor rather than by creditors or by the court. Although the creditors may choose not to accept the debtor's proposed planner and can elect their own, this seldom occurs. On some occasions, the debtor-proposed planner may seek to extend the proceedings by proposing unrealistic or unacceptable plans.

Still another management change may occur when the plan is approved and the plan administrator, described below, takes office.

*□ **Provision of new money.** Businesses in restructuring frequently need new capital in order to operate. Lenders are often willing to provide that capital, but not unless they are assured that their loans will be afforded a first priority in

¹² Nipaporn Weskosith, Steven Miller and Nicholas Poole, *Thailand*, a chapter in *Insolvency & Restructuring 2002*, chapter 28, at page 193.

repayment. While Thai law permits the planner to incur debt (by way of loans, goods or services necessary to operate the business), it does not specifically provide for priority in payment except when the case is converted to liquidation. This statutory omission is ripe for remediation.

* □ **Time frame.** The Thai law provides rather short time limits for all stages of the procedure. As set out earlier, a planner usually has three, and at most five, months to propose a plan. However, the time frame does get extended as creditors propose amendments to the plan. It is not uncommon for nine to twelve months to elapse before a vote on the plan is taken.

* □ **Information to creditors.** The debtor is obliged to turn its financial and other records over to the planner. No public examination of the debtor is required, in contradistinction of bankruptcy cases, in which such an examination is the norm. Creditors must file proofs of claim with the Official Receiver. That officer rules on objections to claims, which may be filed by creditors, the debtor, or the planner. When the planner presents a plan, creditors will be asked to vote upon it. In order to vote according to their best interests, a certain degree of information about the case, the debtor and its prospects should be provided. While some details are usually contained in the plan, Thai law generally falls short in this regard.

* □ **Voting rights and requirements.** The 1999 law increased the complexity involved in the process of plan approval as compared to the original 1998 legislation. Creditors are placed into classes. Each secured creditor with at least

15% of all secured debts must be placed in a separate class, while all other secured creditors are classified together. Unsecured creditors may be placed into one or more classes, although the claims in each class must be similar.

Subordinated creditors comprise still another class. Once the plan has been proposed, the Official Receiver calls a meeting of creditors for the purpose of voting as well as for the purpose of determining whether any amendments are necessary or desirable. A plan is approved by special resolutions of the classes of creditors. That means that at least 75% in value and 50% in number of those voting in each class have voted in favor of the plan. However, if not all classes approve by special resolution, the plan may still be approved if at least one class passes a special resolution, and the members of that class who voted in favor of the plan hold at least 50% of the debt of all creditors who voted on the plan. This latter method of approval is similar to cramdown under Chapter 11 (that is, confirmation of a plan even if not all classes vote in favor). A creditor who votes against the plan may object. Once the plan is approved by creditors, it must be approved by the court. Court approval makes the plan binding upon all creditors.

* □ **Basic requirements of reorganization plans.** A plan must contain, among other things, a description of the reasons for reorganization, a description of assets and liabilities, and a description of the manner in which classes of creditors are being treated. Thai law contains a best interests of creditors test; that is, to approve the plan, the court must find that creditors are receiving at least as much under the plan as they would receive if the debtor were adjudged a bankrupt. In addition,

the debtor must no longer be insolvent. Many plans contemplate nothing more than a rescheduling of liabilities, postponing the day of reckoning by including an unrealistic balloon payment that comes due at the end of the term of the plan.

* □ **Supervision of the process.** Once the plan has been approved, a plan administrator is appointed to oversee the implementation of the plan. A creditors committee may be appointed by creditors after the plan is approved to monitor the plan's implementation process. When the plan has been successfully completed, former management and shareholder rights are restored.

* □ **Conversion to liquidation.** If the rehabilitation process fails, it is not a simple matter to place the debtor into liquidation. For this to happen, there must have been a previous petition seeking liquidation pending before it was stayed by the filing of an application seeking rehabilitation.

The liquidation statute has in many respects not kept pace with recent developments, and thus is not always able to satisfactorily serve one of its most important functions to encourage companies to use the informal or formal reorganization process. A creditor must petition for bankruptcy and demonstrate that the debtor is insolvent on a balance-sheet basis. If that showing is made, a receiving order is entered by the court, and the debtor's assets are vested in the Official Receiver. Thereafter, a meeting of creditors is called and the debtor is examined. At this meeting, it is for the creditors to decide whether the debtor should be adjudicated a bankrupt. The debtor may make a proposal for a composition, which may be accepted by special resolution. If it is not accepted,

the debtor is adjudicated a bankrupt by the court.

Thereafter, the Official Receiver collects the debtor's assets and, in addition, is empowered to set aside certain pre-petition transactions. The Official Receiver will examine claims, object to those that are objectionable, and thereafter distribute the property of the estate in accordance with the statutory priorities.

The conditions described in Part I.B above that appertained when the Asian financial crisis began seem still to apply in some degree today. Family influence and governmental intervention are believed by many to distort the reconstruction process. The ability of recalcitrant debtors to cause delay by numerous and repeated lawsuits is a continuing impediment to the efficient working of the system. The TPI saga was pointed to by many as the prime example of this phenomenon. There, at least 30 complaints have been lodged against TPI's planner and plan administrator by TPI's management, and arrest warrants have been issued against executives of the plan administrator. Most of these efforts have been dismissed but they have held up the process.

Many participants in the process fear for their safety, and bodyguards are common.

Creditors are reluctant to attack fundamental business problems, preferring to reschedule debt, pushing the real problems off to some later date. This has the effect of permitting banks to put these credits back on their balance sheets as performing loans, thus hiding the severity of their own problems.

However, there have been a number of positive results, including the consolidation of the troubled steel industry.

B. Institutional Arrangements.

1. The Central Bankruptcy Court.

Thailand's Central Bankruptcy Court came into existence in June 1999. The Court has exclusive jurisdiction over all liquidation and rehabilitation cases and over all civil proceedings related to those cases. The 21 judges of the Central Bankruptcy Court are rotated in and out of the court. The rotation process minimizes the efficacy of training programs that have been designed to enhance the judges' ability to deal fairly and wisely with the matters that come before them. The Court has its own procedures that are governed by the Act establishing the Court as well as by Rules promulgated in 1999 pursuant to section 19 of that Act.

The Court has been assigned the task of moving bankruptcy cases through the system as quickly as possible consistent with adequate attention. One of the most important results that can come from the Court will be its influence on informal restructurings. If debtors and creditors can predict with some certainty what will happen if a formal proceeding is instituted, they might be more willing to reach an out-of-court deal. If, on the other hand, debtors perceive that the courts are being too lenient with debtors in formal proceedings (e.g., the planner turns out to be an ally of the debtor), or that delay is the norm, they will be much less reluctant to take hard positions in out-of-court negotiations and more willing to institute a voluntary rehabilitation proceeding.

2. Informal Mechanisms: CDRAC.

Even though the law provided for a court-supervised rehabilitation procedure, most restructuring negotiations still took place outside the judicial system, mostly because of the delay that seemed inherent in the latter. As one commentator put it, the pace of restructuring

remained slow, even after the legislative reform.¹³ The need for a more expeditious out-of-court mechanism to effectuate corporate restructurings resulted in the creation of the Corporate Debt Restructuring Advisory Committee (CDRAC), established under the aegis of the Bank of Thailand in 1998. As a consequence of initiatives promoted by CDRAC, in March 1999 a number of Thai and foreign financial institutions became parties to a Debtor-Creditor Agreement and an Inter-Creditor Agreement. Many debtors, financial institutions, and other creditors signed onto the agreements. These documents provided a framework for workouts, adopting the best practices guidelines of various earlier initiatives, including the Bangkok Approach, a set of principles broadly modeled on the London Approach of the Bank of England.

The Bangkok approach that formed the template for CDRAC's work was summarized in the Framework for Corporate Debt Restructuring in Thailand, a product of numerous public and private institutions. The Framework set forth 17 principles that were to guide debt restructurings. In addition, an appendix set forth a timetable to be followed in restructuring procedures, as follows: (i) a meeting of creditors is to be held on seven days' notice. At that meeting a creditors' committee and a lead bank are to be appointed. (ii) Within seven days, the debtor's management is to submit detailed financial information and, upon the request of creditors, independent experts, such as accountants, are to be engaged. During the entire process, the debtor is required to submit such further information as is requested by the committee. (iii) Within three months of the first meeting of creditors, subject to an additional two month extension, the plan is to be submitted to all creditors. Ten days thereafter, creditors may propose

¹³ Lampros Vassiliou, *Legal Issues: Thailand*, appearing in *Guide to Restructuring in Asia 2001*, at p. 126.

amendments to the plan. (iv) Finally, creditors are to decide whether the debtor should be reorganized privately, formally reorganized under the Bankruptcy Act, or liquidated.

As stated in Vassiliou, *supra*:

These [CDRAC] agreements are binding contracts that commit the signatories to follow a framework to expedite debt restructurings. The agreements bind the creditors who signed up to the terms for all debtors that subsequently sign a Debtor Accession agreeing to be bound by the Debtor-Creditor Agreement.

The agreements establish a process to disclose information, prepare and approve a restructuring plan, mediate debtor-creditor disputes and arbitrate inter-creditor disputes. . . . The CDRAC process begins with a first meeting of creditors to prepare a workout schedule and appoint a Lead Institution that helps to co-ordinate the process. A steering committee of creditors may be appointed . . . The process has, in practice, been very time compliance focused with often inadequate attention paid to the quality or feasibility of restructuring deals.

Id. at 128-129.

Once the parties have agreed upon a plan, it is put to the vote of the creditors. If there are significant holdouts or other reasons exist, the court process may be used to approve the plan in a process very similar to that by which a prepackaged plan is approved under chapter 11.

There were numerous problems with the CDRAC approach. Creditors were seemingly unable to make the hard decisions, choosing instead to postpone the problem to another day. Put another way, creditors did not force the debtor to undertake substantial left-side-of-the-balance sheet reforms, focusing only on right-side-of-the-balance sheet debt rescheduling.¹⁴ Conversations with a number of participants in the process confirmed this conclusion.

The latest statistics concerning CDRAC's work, published by the Bank of Thailand in

¹⁴ The same observation was made in *Insolvency Systems, supra* n. 1, at 9, in which it was observed that participants in the Sydney meeting referred to earlier noted certain debtors and creditors have engaged in band-aid reconstruction by only rescheduling debts without attempting real restructuring.

October, 2002, show that CDRAC successfully restructured 10,272 debtors involving 1,364,675 million baht, while 1,671 restructurings involving 419,851 million baht failed.

CDRAC is no longer undertaking new matters. It had a defined life span, which has expired. CDRAC was not renewed because the new government believed that its initiative, the Thai Asset Management Corporation, would facilitate restructurings without the need for CDRAC. It is to the TAMC, therefore, that we now turn.

3. The Thai Asset Management Corporation.

_____The most significant recent development by far has been the creation of the Thai Asset Management Corporation (TAMC).¹⁵ TAMC came into existence on June 9, 2001. In very general terms, TAMC was created to speed up the process of dealing with non-performing loans (NPLs). It is a state agency, all of whose shares are owned by the Financial Institutions Development Fund (FIDF). At some future date, TAMC may issue additional shares that could be sold to the public.

TAMC is in the business of purchasing NPLs from government-owned and private Thai financial institutions, attempting to restructure those loans but, if that proves impossible, undertaking other action in accordance with its mandates.

TAMC is managed by a board of directors appointed by the Minister of Finance and approved by the Council of Ministers.

The guidelines governing purchase of NPLs is rather detailed. The most notable points

¹⁵ See, generally, the detailed analysis of TAMC prepared in October, 2001, by Siam Premier law firm that may be found at its website, www.siamlaw.co.th/publications/tamc/htm; Cynthia Pornavalai, *Thai Asset Management Corporation: Objectives and Powers*, Int'l Bus. Lawyer 174 (April 2002); and The World Bank's *Monitor*, April 2002, at 36-37.

are:

- * □ All NPLs classified as substandard in government-owned financial institutions or asset management companies must be transferred to the TAMC. A transferor may not pick-and-choose which NPLs to transfer.
- * □ NPLs of privately owned financial institutions or asset management companies that are of sub-quality can be sold to TAMC only if they are collateralized.
- * □ Non-Thai institutions are ineligible to transfer NPLs to the TAMC.
- * □ Certain provisions contained in the decree make it difficult for private institutions to refuse to take part in the TAMC scheme.
- * □ The overwhelming majority of NPLs transferred to the TAMC have come from government owned institutions. This may be due, in part, to the fact that many of the NPLs owned by private institutions had been part of the CEDRAC process. Another reason is that the pricing for NPLs transferred by state-owned transferors is more favorable than that offered privately-owned institutions.
- * □ The purchase price of the transferred NPLs is paid by 10-year non-transferrable notes guaranteed by the FIDF. A formula exists with respect to sharing of any gain or loss on the transferred NPL between the transferor and the TAMC.

TAMC has been given extraordinary powers with which to enforce its mandate. It has the powers to restructure debt, reorganize the debtor s business, dispose of the debtor s assets, and may foreclosure security interests without the necessity of instituting judicial proceedings. There are very few restrictions upon the way TAMC may accomplish these tasks. The debtor s consent is not even necessary in some cases. For example, with respect to debt restructurings, TAMC

may extend maturities, reduce principal or interest, convert debt to equity, receive title to the debtor s assets to reduce debt, or engage in any other transaction that is deemed appropriate.

There are some restrictions upon TAMC s ability to reorganize the debtor s business. Some of these are reminiscent of the criteria for rehabilitation under the Bankruptcy Act. These restrictions are: (1) the debtor must be a juristic person; (2) TAMC must own more than 50% of the debt; (3) there must be a reasonable prospect for rehabilitation; and (4) the debtor must consent. If any one of these facts is not present, TAMC lacks the power to reorganize the debtor s business. Any reorganization would then have to be done under the Act, if that statute s eligibility criteria are satisfied.

If the debtor s business is to be reorganized, TAMC must follow a program that again is quite similar to that found in the Bankruptcy Act. If a reorganization is agreed to, a planner and plan administrator are appointed, there is a time limitation for implementing the plan, and the plan is, when all is said and done, submitted to the Bankruptcy Court for approval. In this sense, the process is similar to the prepackaged plan found in the United States.

According to a recent press release,¹⁶ 800 cases having a book value of 292,922 million baht had been concluded as of the end of August, 2002. This is up from 357 cases involving 134,252 baht in book value at the end of May, 2002.¹⁷ Of the 800 cases, 349 cases with a book value of 134,252 million baht (46%) were approved for debt restructuring, while 51 cases with 14% of book value had gone through business rehabilitation in the bankruptcy court, and 390

¹⁶ The press release, No. 9/2000 (12 Sept 2002), as well as other information concerning the operation of the TAMC, may be found at <http://www.tamc.or.th>.

¹⁷ Press Release No. 7/2002 (7 June 2002).

cases with 38.6% of book value had undergone foreclosure or receivership. Of the cases that had been concluded, 31.7% by value were in the real estate sector and 28.1% in manufacturing. One other interesting statistic, gleaned from an the earlier press release, is that about twice as many cases involved single-creditor loans as opposed to multiple-creditor loans. TAMC counts among its successes the successful restructurings of Advance Paint & Chemical (Thailand) Plc, Thai Cane Paper Plc, and Thai Copper Industries Plc.

Other information contained in TAMC publications or on its website reveal that it intends to use joint ventures and special purpose vehicles, among other things, to resolve cases. Its case-by-case evaluations are made with the help of financial advisors.

Outside observers tend to have reservations about the present and future effectiveness of TAMC. There is a developing consensus that: (1) TAMC is rescheduling rather than restructuring, with the result that it is merely postponing, not solving, problems; (2) it does not yet have the personnel necessary to accomplish its tasks; (3) the published statistics tend to overstate its performance;¹⁸ (4) it is rather slow; and (5) it is not transparent enough so as to gain the full confidence of the marketplace.

According to The World Bank's *Thailand Economic Monitor*, May 2002 at 37, part of the problem faced by TAMC is that its approach of balancing the positions of creditors, debtors and taxpayers runs head on into the private banks' approach to restructuring which, according to The World Bank, seeks to maximize recoveries.

Nevertheless, TAMC has created high hopes in the restructuring community. If managed properly, TAMC could be a pacesetter, thereby increasing the ability of financial institutions to

¹⁸ See, e.g., Pornavalai, note 18 *supra*, at 185.

work out their own NPLs.

4. Debt Restructurings Carried Out by Financial Institutions.

Not all NPLs have been assigned to TAMC. A good deal of debt restructurings are being carried out by financial institutions. According to the recent report by the Bank of Thailand, approximately 40 thousand cases, involving 101 million baht, were in the process of restructuring as of 30 September 2002. Approximately 75% of the cases and two-thirds of the value involved state-owned banks; the remainder involved commercial banks. More than 650,000 cases, involving more than 3 million million baht had been completed. By far the greatest number of cases (260,000) involve what is described in the report as personal consumption.

PART III. CONCLUSIONS AND RECOMMENDATIONS

Most experts agree that the Bankruptcy Act itself, despite some shortcomings, is a pretty good law. What is lacking is proper implementation. This due to a multitude of factors.

First, the companies most in need of business restructuring are frequently controlled by families with the power, prestige, and influence to deny governmental and non-governmental institutions the power they need to liquidate businesses that need liquidating, restructure the business of companies that need restructuring, and reschedule the debts of enterprises that have sound businesses but may have temporary cash-flow problems.

Second, as strange as it seems, these problems are not being faced in part because of the improving economy. This leads to the perception that the Asian Financial Crisis is all but over, and that all the distressed companies need is a little more time to rise with the tide of increased sales and a booming Thai economic environment. The problem, of course, is that no economic trend goes up (or down) forever. Sick or mismanaged companies do not become healthy or well-

managed just because times are better. Underlying systemic problems will have to be addressed at some point, whatever the economy is like, and many of the enterprises whose debts were merely rescheduled will predictably return for further relief. Indeed, the best time for reform is when the system is not under pressure.

That said, there is nevertheless cause for some guarded optimism. Bank underwriting standards are slowly improving, as are bank regulatory practices. A goodly number of Thais have been trained in the business of restructuring, and one can look forward to their increased participation in the next round of restructurings and rehabilitations. Company managements, while still reluctant to lay off employees or modify business practices, may nevertheless be more cautious about adding more staff just because times are better.

The Central Bankruptcy Court is one of the real bright spots in the insolvency scene. However, its own statistics reveal that a large number of cases remain pending. It still needs improvement so that it might become more efficient. More training and increased spending on technology are immediate needs. The Court (and Thai courts generally) seem reluctant to act expeditiously in any event, and particularly in cases involving creditors attempting to enforce their rights. Debtors are given too much free rein to clog the system and add to the delay.

There is a broad consensus that the Bankruptcy Act needs to be modified in some important respects, as follows.

(1) The type of insolvency that permits access to the bankruptcy system should be modified to include equitable insolvency (inability to pay debts as they mature) as well as balance sheet insolvency (assets are less than liabilities). Perhaps the standard should be different for voluntary and involuntary cases.

(2) The status of post-petition debt incurred in operating a debtor's business needs to be clarified and a priority afforded. This should lead to the increased availability of capital for companies operating in a formal reorganization proceeding and perhaps make restructurings easier to accomplish.

(3) If rehabilitation fails, the ability to put the debtor into bankruptcy needs to be made easier. Perhaps conversion to bankruptcy should be automatic unless a party in interest shows cause why dismissal of the case or some other remedy is appropriate. As it is, the difficulty of converting a case to bankruptcy permits insolvent and unviable businesses to continue operating.

(4) The potential that the important players in a restructuring may incur personal liability discourages many qualified people from participating as planners, plan administrators, or acting in other roles. This possibility might even extend to employees of TAMC. It certainly inhibits bankers employed by state banks from making decisions for fear that, if their decisions turn out not to have been correct, their personal estates might be jeopardized. Legislation should be enacted to restrict personal liability to grossly negligent or fraudulent conduct.

(5) The recent process of licensing insolvency practitioners, starting with planners and plan administrators, has had decidedly mixed results. While many believe that licensing enhances the quality of those involved in the restructuring process, the new regulations require that planners must be Thai and that corporations that are planners must be Thai-owned and have a prescribed majority of Thai employees. If a planner is not licensed, a substantial bond is required, a requirement not easily satisfied. This has led to the development, noted above, of debtors becoming their own planners, because debtors need not be licensed or bonded. It is too early to reach any conclusions about the licensing process itself, because the licensing committee

has only recently started its work and there have been few applications.

(6) There is some disagreement as to whether the current law favors debtors or creditors. Because it is so hard to separate out the effects of the law from the effects of the way that the law is administered that it is almost impossible to determine which side of this argument is stronger. Studies are underway to determine if a debtor-in-possession scheme should be created.

(7) The need for a new law dealing comprehensively with secured transactions is apparent. Statutory reform is needed with respect to types of property that can be taken as collateral and with respect to the manner in which perfection may be accomplished. At the same time, immediate and comprehensive reform in the ability of secured creditors to enforce their security interests is imperative. Speedy remedies frequently force debtors to face up to their problems sooner rather than later, resulting in timely, not delayed, remediation. The World Bank's *Thailand Economic Monitor*, May 2002 at 35 points out that the pace of restructurings has been undermined by the backlog of cases in the Civil Courts, where mortgages are enforced. According to the *Monitor*, there are **65,000** NPL cases awaiting judgment, a process that will take **seven** years to clear up, assuming no new cases.

(8) Substantial improvements are needed to make the debt collection process speedy and relatively inexpensive. At the present time, it is next to impossible to obtain a judgment and proceed to execution on an unsecured claim in anything approaching a reasonable amount of time.

One of the distinct trends that became evident during the author's conversations in Thailand and elsewhere is the departure of the Westerners who were instrumental in getting the

system off the ground in 1997 and who trained the Thais in the restructuring business. Part of the reason for this is just the normal course of events. Some allege that the corruption endemic to the system (family influence and governmental intervention, as described above) has driven them away.

Substantial progress has been made in Thailand, which was one of the first countries in the region to tackle head on and in a bold way the issue of insolvency immediately after the Asian crisis. But more needs to be done and there is a sense that the longer these needs are not addressed the tougher it will be to address them down the line.

Whether an optimistic view of the future is warranted will be discovered only when the next round of restructurings commences, whether they be re-entry or new NPLs. Will serious attention be given to restructuring the business? Will liquidation be forced when liquidation is called for? Will fine distinctions about how to treat differently situated businesses be recognized and acted upon? Will much-needed legislation be enacted? Will the irreversibility of reforms that have already been undertaken be guaranteed in the future? These are the key questions that need to be answered in the months and years to come and upon which hinges the success of the Thai approach to insolvency reform.