

UNCITRAL/INSOL/IBA GLOBAL INSOLVENCY COLLOQUIUM

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EVALUATION AND SYNTHESIS SESSION

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(edited transcript)

PANEL

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Justice FARLEY

Good morning. The evaluation team has reviewed all submissions and has concluded that the objective we should strive for is to work out the elements of a functioning insolvency system which will maximize the utility of the tangible and intangible assets of an enterprise on a fair and balanced basis to the stakeholders affected on a timely schedule. Financial failure, absent fraud or its equivalence must be recognized as a dynamic of a healthy competitive economy. The insolvency system provides for the recycling of the assets on a non-wasting basis. Transparency and certainty going into the relationship and in going into and coming out of the insolvency condition assisted by suitable information standards and information access are important to allow for predictability, since uncertainty of result leads to delay in resolving issues. The system should be understandable by both domestic and foreign participants. With delay there is the erosion of value as uncertainty or gaps provide for inappropriate opportunities for posturing rather than legitimate bargaining, including provision of interim financing necessary to maintain value. Even within an informal insolvency proceeding, recognition that one is operating within the shadow of the law in a functioning insolvency system will result in the informal and timely resolution of issues. The insolvency system will involve a liquidation channel when that is the way in which the resources of the enterprise can best be employed, but with a reorganization channel if that is viable and will result in greater value. Viability must be viewed on a foreseeable future basis and will likely involve rehabilitation of elements of operations, management and/or recapitalization (of both debt and equity). The process of rehabilitation will require flexibility in approach to best suit the prevailing circumstances.

It has to be a functioning insolvency system which is understandable, including the recognition of its impact in other areas and what is suitable to the stage of development of the particular jurisdiction, subject to review and appropriate change as the development stage

evolves. “Functioning” and “system” also denote that the insolvency system is more than a set of laws on paper. There must be a facility to allow the debtors and the creditors in the business community and their advisers and, if insolvency occurs, the participants in the insolvency process including lawyers, insolvency practitioners, work-out managers, regulators and courts, to understand how the system works in practice and their respective roles and interaction.

The insolvency law will be pervasive in the insolvency system, but the system will not work unless it has the requisite talent to activate the process and keep it energized to its more suitable conclusion. The racing car may be well designed but needs a skilled driver and maintenance crew plus gas. The proof of the pudding will be in its eating. On reflection, has the insolvency system worked, so that resources have not been wasted when viewed from a neutral observer’s position? Has the system worked optimally for the particular known culture of that jurisdiction?

Because of the mandate of UNCITRAL, the Working Group will be developing a strategic plan for the framework of the insolvency law. However, there must be recognition and appreciation that the other building blocks of the system must also be present to allow proper functioning. The evaluation team is of the view that the UNCITRAL process should not be dragged out. Rather the two additional “Ps” of “progress” and of what is “possible” dictate that this time frame should be two years. With a changing appreciation that rehabilitation, if feasible, will likely result in the maximization of value, we expect that this emphasis will be important. Notwithstanding the limited time frame envisaged we do contemplate that this review will presently involve an analysis of the proposal to have introduced into the system an intermediate step between a fully consensual work-out plan and one which is processed over an extensive period of time through the court, tribunal or other neutral system with a view to binding affected parties provided that a particular majority of similarly situated parties confirm a plan which meets certain other objective criteria as determined by such neutral. It is understood that the intermediate step would involve extensive and intensive out-of-court negotiations, but if unanimity were not possible, then there would be a facility to have a “speedy” process with the neutral ensuring that the same safeguards were in place as with the more traditional process. We recognize that while liquidation is a more established channel, we expect the emphasis will be on developing the framework for rehabilitation. That is not to say that there are not important and serious aspects of liquidation which must be addressed, for example what is a logical and practical priority system. We would point out that this concern also impacts the reorganization question. Similarly the liquidation analysis must address the question of whether secured creditors are exempt or are their enforcement rights modified or temporarily suspended.

Economic and social imperatives

Let us now turn to the economic and social imperatives. Any insolvency system to be implemented must have the dedicated knowledgeable support of not only the usual participants who operate within that system. It must also have the appreciation of the legislative, executive and bureaucratic arms of government that it is demonstrably in the public interest to have a functioning insolvency regime with the goal attributes which we have previously mentioned as a means of encouraging economic development and with that the attainment and enhancement of social policy. This is over and above the issue of how effectively to deal with the social network and utility provisions attendant “company towns”

of state-owned enterprises. Richard Gitlin will now take a few minutes to outline the questions of economic imperative and Judge Wisit will deal with social issues.

Mr GITLIN

Years ago Judge Lifland designed what we call a channeling injunction. Any insurance company or others that put money into a solution were freed of claims from others and the claims were channeled to the funds. What impressed me these last couple of days was the enormous amount of talent and experience in this room, and one of our responsibilities is to take that talent and channel it into something that can make a difference. We were cautioned by both Gordon Johnson and Hal Burman to make sure that whatever we do can be put in an economic context, make sure that there is an economic definition, or else we run the risk that we all work very hard but do not accomplish anything. So in a sense part of our effort must be to define the economic imperative of our work. I thought I would spend a minute on the economic imperative.

If you look at what has happened in the last few years, the IMF has acknowledged that in its initial efforts in Asia it did not fully appreciate the significance of corporate restructuring. The World Bank has spent enormous resources studying this area and it is quite impressive that bankers, bondholders, and noteholders, who really do not usually spend a great deal of time outside of their businesses, have spent an enormous time under the leadership of Adrian Marriette and Terry Bond in designing out-of-court principles for workouts. And what you realize, listening during the last couple of days, is that just about every country in the world is studying rescue systems.

I recently participated in a conference in Japan that really brought this home. The Ministry of Trade and Industry created a conference that dealt with balance sheets and economic recovery. This is the first time I have ever really seen economics and rescue systems put together so that you could define how significant it was to the economy. The reason Japan did this is that they have a new rescue law (April 1st 2000), but real rescues are not taking place, rescues that include debt-equity conversions, fixing the company, fixing the balance sheet and resetting the strategy. So until the rescue priority gets into policy and politics, you will not get the rescues in Japan.

If you look at where it fits in an economic cycle, what you realize is that a proper rescue system is absolutely critical to financial rehabilitation either in a recession or a crisis. Just look at one simple situation - there is a company with a loan and it is not able to pay the interest and maybe the Bank is loaning more monies to hide the fact that it is a non-performing loan. But the company has more debt than it can pay and therefore cannot borrow any additional money to invest in its future. What happens to that one company? It goes down in value because it cannot compete. You cannot compete today if you do not invest. What happens to the Bank, that holds the note? It goes down in value because the company that owes it money becomes less valuable. And what happens to the economy? It goes down in value because you are not investing in new employment and new equipment. Now take that one situation and multiply it by a hundred thousand in a particular economy and feel the economic impact of not having a rescue system in place. So number one, a proper rescue system it is a critical component in accelerating corporate recovery and economic recovery.

The second part is we have clients who buy bonds around the world now coming to us asking us to compare rescue systems for purposes of pricing their loans in the capital markets. They say they do not know the difference between pricing the rescue systems in Columbia, Argentina, Mexico and Chile, but they need to know that now. So a rescue system will affect the pricing of capital. And the third is, we found in London recently, that governments are concluding that having a good rescue system is a critical component to entrepreneurship; venture capital flows better if there is a process to resolve failure because probably five out of six venture capital investments fail. It is unlikely that significant money will be invested in a situation where there is no viable rescue mechanisms to deal with the losers. If you add this up, there is a compelling economic argument for the work that we are about to commence. The improvement of rescue systems should be moved up the list of economic policy and political priorities.

Judge WISIT

In looking at a uniform law or other product in order to ensure that insolvency law in the world is better, we must not lose sight of the importance of the social impact of the bankruptcy law. In many countries, as we learned from some delegates, bankruptcy laws are not used or perhaps only rarely used, or are perhaps very difficult for creditors to use. In looking at the cause of the failure to use the bankruptcy law, it is not simply that the law is bad. Perhaps we need to take into account the social status of the bankruptcy law in different countries. In some countries, being bankrupt means that you cannot work, you have to lose everything because you are a bankrupt or used to be a bankrupt. So in considering the process of developing either a uniform model law or uniform model provisions, perhaps we may have to bear in mind that in some countries bankruptcy has a very strong social impact.

Key elements of laws and issues related to infrastructure

Justice FARLEY

Any insolvency law will have to include certain key elements in order to operate. While it would be impossible to discuss all the presently identified suggestions, they are exemplified by the points set forth in the appendix to this report. Members of the evaluation team will highlight considerations and elements which are involved as to developing means and implementation in a law. These elements cannot be viewed in isolation; they must all interact smoothly in a functional system. The selected pieces must fit. Nor can they be developed in isolation from the other building blocks of economic or commercial law. They must interface effectively with these other areas. The linkages must be shown on a basis of allowing the system to work. The pros and cons and implications of each choice must be recognized on a focussed basis. As well, they will be affected by other elements of government concern, as insolvency law is woven in the general fabric of each jurisdiction's laws which will differ according to their individual cultures.

Ms WEE

We have heard Justice Farley and Judge Wisit speak about some of the social issues as well as the role of UNCITRAL. Yesterday we heard quite a few delegates stress the importance that any work undertaken by UNCITRAL not be segmented and fragmented. And that the issues must be looked at in a holistic manner, including linkages with other

aspects of commercial law. I mention this again because it impacts on how UNCITRAL will have to look at elements related to eligibility, commencement and access. The scope of review of an insolvency framework will need to include the review of important policy considerations regarding the scope of application. Such as, whether to include, for example, banks, insurance companies and state-owned enterprises. I liked Jane Marshall's caution yesterday of a Government health warning. Possibly we need to put a big red light – a Government health warning - if SOE's are included in the scope of an insolvency framework - that there might be important social considerations which will need to be highlighted. Also cultural sensitivities and compatibility with the social fabric, as well as the purposes and goals of the insolvency law, as it relates to that particular society, will all need to be reviewed for their impact on eligibility criteria.

With regard to commencement, realistic entry criteria, fairer entry criteria and creditor's rights to initiate proceedings, appeared three times on that list we considered yesterday. It became obvious from listening to the experience of Nepal that not all countries have entry criteria that are ideally suited to modern business practices. Therefore, the evaluators have concluded that there are important policy choices to be made here. For example, whether countries are trying to encourage early restructuring and whether the concept of debtors' prison is to be discouraged. What kinds of tests are applicable? Is it the balance sheet test, liquidity test, or a cash-flow test? All these are issues where considerations of policy will have to be stressed. The commentators consider that it is important to ensure that whatever is considered in the forthcoming work of UNCITRAL will not stifle innovation. As was mentioned from the floor yesterday, modern banking instruments and accounting standards are badly considered. And if what we are trying to encourage is a process that is quick, friendly and efficient, then recognized tests of insolvency must be encouraged.

Access raises some fundamental policy issues such as better integration between insolvency and rehabilitation laws. Yesterday it was mentioned that a clear insolvency law as a backdrop to rehabilitation is the necessary key element to any functioning insolvency system. The policy choices relating to whether there is to be a separate or dual process will need to be explained. The choices relate to the points at which conversion from liquidation to rehabilitation will need to be explored. Some of the issues that will need to be considered by UNCITRAL as it goes forward in this particular area will be to address the effects of globalization and change. In light of the overwhelming systemic levels of insolvency, one of the fundamental issues will be whether a single process has now become outmoded. With respect to the issues of moratorium and stay, the questions are how broadly a stay will apply and when it commences. In many countries the stay does not automatically commence. It commences possibly a month to three months after the commencement of the filing of any case. Is that desirable? And how long does the stay apply for? And how wide should this net be cast? Should secured creditors, for example, be included in such a net? What are the other commercial laws that may impact on this particular issue? Again we heard caution from the floor and perhaps another Government health warning and red light is needed here with respect to the linkages with debt enforcement mechanisms.

Mr ZAHARIEV

In my short summary, I will try to focus on two aspects of the list of issues that we have outlined, that is the role of management and the role of creditors and creditors' committees in terms of the key elements of an effective insolvency regime. Starting with the

role of management, I believe the sense of the meeting was that one of the identified needs was to distinguish between the role of management in insolvency proceedings in general and in liquidation. I think there was agreement that in liquidation, management personnel should be removed and the entire management should be placed into the hands of a liquidator whose rights and responsibilities should be regulated clearly by the law. As to insolvency proceedings in general, at initiation (the first phase before liquidation is decided, if it is decided) the law should focus on the relative responsibilities of creditor- or court-appointed bodies such as trustees in bankruptcy, interim managers and the existing management, and ensure the option of the creditors to remove the existing management, if necessary. That is certainly one of the practical experiences that our institution as a lender in private sector projects in difficult areas, has learned - sometimes there is a need to remove immediately the existing management in an extremely controversial situation where there is fear of dissipation of assets and possible other adverse consequences. In other situations, where management may be cooperative, it should be supervised by a lender-appointed trustee or court-appointed trustee but could continue to run the day to day business of the company, because that is a cost efficient solution. I believe also that the sense of the meeting was that there is a need to strengthen the responsibility of management, especially in the sense that there is a need to clarify and strengthen liability for insolvent trading. The assumptions made by specialists and practitioners from Anglo-Saxon systems about the self-evidence of that responsibility is certainly not reflected in reality in many parts of the world, so that any legislative guide prepared by UNCITRAL should at least sharpen the focus of legislators to the need to pinpoint and clarify the liability for insolvent trading. I believe that this will also be an important incentive for management to negotiate more permanent rescue solutions with their creditors rather than attempt muddle-through scenarios until it is too late.

Moving us to the role of creditor committees, one of the findings of the meeting was that the role of the creditor committees is well described in existing documents, such as the World Bank and the IMF reports and that the work of UNCITRAL can certainly build on existing expertise in this field. I believe that the sense of the meeting was that there is a need to clarify and distinguish the rights of various classes of creditors, in terms of participation in creditor committees and voting rights, and that the rights of various creditors including secured creditors should be fairly reflected in the provisions relating to the role of creditor committees. A next point was that legislators should be reminded of the need to ensure legal certainty for the members of creditor committees. That is also something that my institution has often faced. Being usually amongst the larger creditors of an insolvent debtor and having also a certain weight and influence in the region, the EBRD is often asked to participate in creditors' committees and we sometimes face uncertainty as to the liabilities attaching to being a member of such a creditors' committee and how those liabilities are discharged, indemnified or regulated. So that is also a point that probably needs to be highlighted to legislators if UNCITRAL goes the route of developing a legislative guide.

Turning to the role of creditors in general rather than creditor committees, I believe that the sense of the meeting was very strongly in favour of recognizing that it is necessary for UNCITRAL's work to emphasize the fact that the creditors are the primary stakeholders in the process of insolvency. Any modern insolvency regime should recognize that there are other stakeholders in the process, that it is not only about creditors - we spoke about the social impact on workers and maybe their special priorities as a matter of policy, about the rights of other stakeholders such as shareholders and the community at large, such as tax payers. However, the legislator should never lose sight of the fact that the whole process of insolvency is, and should be, creditor-led; that the primary stakeholders are the creditors; and

that the whole process is about maximizing, as efficiently as possible, the value of the enterprise which can be efficiently recycled into the economy for the benefit of creditors. And that flows through the entire process of insolvency. It goes further in terms of the need to remind legislators that control of the insolvency process should be with the creditors, that for instance, court supervision should be quick and efficient and always available as an option to the creditors and to all other stakeholders. However the whole process should be creditor-led and the same applies to the choice of liquidator, or even before the choice of liquidator, to the choice of an interim manager or trustee in bankruptcy. The same also applies to the right to propose a plan for restructuring or rescuing the borrower, to negotiate that plan and to approve that plan.

Now I believe there is also a further understanding that emerged from the discussion and that was seen from the economic perspective of emerging markets and developing jurisdictions. That was the need to focus on the fact that bankruptcy is one of the elements of ensuring credit to the economy, including foreign investments by foreign lenders and that, whilst a bankruptcy system should of course secure the rights of creditors to private persons and to various other creditors, bank lending has a special role in the economy and that the needs of bank lenders as creditor should be adequately reflected in an effective insolvency regime. That applies to both local lenders and to foreign lenders, however the special issues that arise from lending in foreign currency in inflationary economies should be recognized in the bankruptcy process. A modern insolvency regime also needs to take into account certain standard provisions of Eurocurrency loan agreements that are used by foreign creditors such as grossing-up clauses and default interest clauses which affect the quantum of the claim of a foreign exchange creditor. I believe that this probably summarizes the findings of this meeting in respect of the role of creditors and the role of management.

Judge ZULMAN

I would like to focus on rehabilitation and how we should go about designing an effective regime to deal with the matter. I believe that what came out of the discussions was what we need to look at as the main topics. Firstly I think one needs procedures to be established so that rescue proceedings move forward on a timely basis, I stress timely, and that parameters be established for the submission of proposed restructures by the business, by the creditors' committee or an administrator appointed by the court. I think you need to achieve a balance. I am reminded this morning that the balance between Gore and Bush is apparently an even balance; they each had three thousand lawyers on their respective sides. You need to have a balance so that you can deal fairly with these different interest groups. I think what Richard Gitlin mentioned in one of our discussions yesterday, the idea of laying a table and getting people to that table to know what is on the board, is also very important.

Laying the table requires information so that when creditors come to the table they know what is going to be served up on the menu. If you are not informed as to what the rehabilitation compromise of the scheme of arrangement is about, there will be problems. You need some sort of guideline which obliges you to set out to what is going to be needed. Linked to this is the requirement of financial information that is meaningful and that enables creditors to weigh up what is good or bad. What we talk about, following English precedent, is the sea of certainty, that out of a compromise or a restructure you are going to get something certain. By contrast, in liquidation proceedings you may end up with either very little or maybe slightly more, but there is an element of uncertainty which is eliminated by a proper rehabilitation scheme or a reorganization scheme. That message seems to come out

clearly in the sessions Ron Harmer conducted; one needs to bear in mind the seven principles which were distilled by him in addition to the various “P’s” that were raised in the first session.

First of all I think what you need as a backdrop is a clear insolvency law so that one knows precisely, or as close as one can, what is going to happen. Certainty of payment to the professionals is important; people come to work a bit better if they are rewarded, work a bit less better if they are not rewarded, or work in a bent fashion if they are inadequately rewarded. You need realistic entry criteria to get to the table to participate, you need to balance, as I have mentioned, the rights of the different parties, and you need understandable legislation. There is the problem of writing legislation in terms that even laymen can understand and it’s a very difficult proposition. I think Bentham thought of that when he suggested that every cab or taxi driver should have a manual of English law that he could instantly refer to and understand what it is about.

Should the insolvency law provide for provisions for out-of-court restructuring, I think yes, but my experience has been that it does not always work very well. I think you need an element of the stick, especially to deal with recalcitrant creditors or people who need to be brought to the table, because they can hold out and upset the whole restructuring scheme. It is not a good idea that an economic blackmail gets a better deal than the rest. We still have a system in South Africa of judicial management. It goes back a long way and it really has not worked out because of the problem of expertise which has been raised here. The judicial manager, and I mean no disrespect to the accounting profession, was invariably an accountant who knew very little about corporate structuring in different sorts of business roles. He was not a corporate doctor who could really go into a business and do anything meaningful. What he would tend to do is to leave the existing inefficient management in place, get them to stumble through it, charge an enormous fee for watching over them supposedly and, within the statutory or court established period, bring the judicial management to an end and put the company into liquidation. There were occasional cases where it did work, but that was just by chance. Whether one gets to the American idea of leaving the debtor in possession is a moot question, but I think one really needs to aim at a proper restructuring set-up.

Prevention of abuse

Mr GITLIN

Just briefly, the process of using a court to rescue companies is very odd when you think about it. What do you do when you rescue a company? You are fixing the business and you are doing a business deal. So we move that process into a court and ask the judge, who is usually exposed to a two party dispute, to take this complex business situation and guide it through the process. One of the key functions of the court in setting the framework for this to take place, is to make sure there is fairness. That is why we need a court. So when we talk about preventing abuse - preventing abuse in management, preventing abuse of professionals, preventing abuse of transfer of assets - we need to look to a court for the integrity of the process and to guide the process. Whatever law is developed it must, in all respects, make sure that that is one of the prime benefits of using the court process.

Possible form of UNCITRAL work

Ms CLIFT

I would like to briefly outline the form that the evaluation panel thought work by UNCITRAL could take. As you will appreciate there is a fairly significant amount of background material that could be included in the type of instrument that we have talked about UNCITRAL developing. I am sure as the work progresses, the elements that are included in the instrument or work product will change and develop. But we see three main areas that the material could be organized into. The first area more or less reflects what is the key component of the reports we have seen from the Asian Development Bank, the International Monetary Fund and the World Bank, that is a consideration of alternative policy options and approaches to the different issues that are outlined in the key elements. This part could also include considerations related to social and economic factors.

The second area would be a comparative analysis of some of the provisions and precedents that are already in existence in national legislation and international instruments. That could also possibly include summaries of experience with some of those provisions, to the extent that that experience might be enlightening in assisting legislators to make choices between different policy options. This part, of course, would not be incredibly detailed because the purpose of the instrument is not to provide a large comparative study but, to the extent that outlining the policy options and different approaches and analyzing what countries have already done contributes to the third part, which we think is perhaps the most important, that material would be very useful.

The third part would be what we might term drafting instructions or suggested legislative provisions or recommendations. The form in which that third part appears may very well depend upon the topic that we are talking about. As we noted in our discussions, some of the key elements may lend themselves to actually drafting provisions because they reflect more or less a general consensus that a particular approach should be taken. But where that is not the case, then we might outline what we see as being the key elements or the key points that should be addressed to deal effectively with certain topics. That is just a very broad outline of how we see the material being organized and I have no doubt that it will evolve as the project proceeds.

Judicial and professional training

Justice FARLEY

This of course is part of the infrastructure, the meaningful infrastructure requirements, for a successful operating insolvency system. As discussed, a functioning insolvency system requires that the insolvency law be supported by an effective infrastructure. The most effective system is one in which there is the minimum debate about the likely legal outcomes and the maximum discussion and bona fide negotiation of the optimum methods of maintaining value in a particular set of circumstances; that is not restricted to the insolvency law. There must also be appreciation that the requisite infrastructure is present. We have heard about operating in the shadow of the law, but it is important to operate in the shadow of the operational infrastructure as a foundation upon which that law can be deployed.

Allow me to briefly deal with this question as it affects the courts or tribunal or other neutral. Minimizing dead time is important to avoid unnecessary erosion of value. The court must be capable of being accessed on a timely basis as required. Insolvency is what I term “real time” litigation which must take precedence over what I call “autopsy” litigation, which is not adversely affected if it is dealt with tomorrow, next month or the next year. Necessity dictates that the queue must be jumped but with a reasonable and realistic timetable which has to be dictated by the controller or the judge. The insolvency case must be entrusted to a judge who has a commercial mentality, awareness and approach. He should not only rely upon his own skills and experience, but know how and when to rely upon the business expertise and experience of others in the case. He should be one who has developed experience with dealing with insolvency proceedings and their special needs, including knowing when to allow the affected parties the opportunity to negotiate outside the court, even with recess in the proceedings of a matter which is underway in court. A real time approach requires that the judge make clear and timely decisions, frequently on an overnight basis at the maximum. The decision should be legally and practically sound. Appeal periods should be kept to the minimum, consistent with fairness to the affected parties. The appeal court, especially if it does not have the functional expertise of the lower court, should through experience with that judge, come to appreciate that reversal, in whole or in part, should rarely occur and only when there is a true miscarriage of justice. We recognize that it is not desirable to have insolvency cases randomly assigned to members of the general court. While a specialized court of commercially-oriented judges may be possible, we anticipate that frequently flexibility and accessibility would be enhanced if certain of such judges of the general court were designated to handle insolvency cases, which cases would have a first trial priority as to their scheduling. To the maximum extent possible, the same judge would be involved in the continuing insolvency proceeding. The judge must be the true exemplar of neutrality and the embodiment of the rule of law. Appropriate selection on merit and ability of judges to be appointed in a regime where judges have security of economic well-being and tenure and are accountable on objective standards of good behavior including non-corruptibility is important in developing and maintaining the tradition of the rule of law. The judge must not only possess these qualities but he must be perceived from the outset as being of this calibre. We note that there was significant concern about the training participants in the insolvency system. Judge Wisit will review the infrastructure requirements which will be of particular value, given his experience. Judge Jean Luc Vallens will deal shortly with training as it affects judges, and Claire Wee as to the remainder of the participants in the insolvency process.

Judge WISIT

In this colloquium we have seen the different directions that can be taken in terms of the body that has authority over insolvency cases. In some countries that authority is placed with organizations apart from the court, but we also see that the present trend is to move that responsibility to the judiciary and with this move the court becomes very important in dealing with the prevention of abuse. The question would be how can we ensure that we have committed judges to deal with these cases; the answer is hard to find when you are trying to build the system afresh. Training, as we have heard from many participants, can raise knowledge and awareness, but experience can only grow over time. In trying to set up the system there are many questions that we have to tackle: should the judges be specialists, should the system provide more opportunities for them to gain experience and should the court be specialized. In any event, this will have to be dependent upon the decision of each country. Experience has shown that to build up the system as quickly as you can, to get to

the target set by many participants, is not an easy task. But one thing that we have to bear in mind all the time is that judges should be treated with respect and they should be fairly paid within the system in order to prevent corruption.

Judge VALLENS

Training of judges is a big deal. Let me give some minutes to this very important but sensitive subject. In the last 2 days, many participants have recorded a real need for training of judges involved in insolvency work. Obviously, material resources are necessary too, as they are a pre-condition for judges involved in such cases to be able to produce good results. And as has been said before, the independence of judges is important and they need to be afforded regular protection against pressure or lobbying. While training of judges is obviously outside the scope of insolvency laws, it is necessary as a pre-condition for making insolvency law work well, which is our goal.

Now what does it mean to train judges in insolvency matters? We can focus on two issues – the first is why we need to train judges and the second is what is that training directed towards.

The first assumption, shared by a lot of us, is that judicial control is absolutely necessary for the insolvency process, for many reasons, including to ensure fair treatment to all the parties, to grant the right of petition at law, and to provide legal certainty to third parties, creditors, lenders, foreign or local lenders, the state and debtors too. Such control needs to be accepted and efficient. The judge has to know what he or she has to do, and understand economic mechanisms, macro- and micro-economics, so that they understand quite well the rules of the matter and the purpose of insolvency proceedings. They need to be able to avoid prolonging the proceedings, because it is a very important matter for us not to spend too much time before reaching decisions. Accounting, too, is important so that judges can understand balance sheets, appreciate insolvency data and so on. When a court has to determine the best solution for a troubled company, it is quite difficult to do so without understanding its cost accounting and its estimated budget. Training is also necessary in financial rules, to assist in decisions whether or not to approve composition or rehabilitation plans and should focus on technical matters, such as the consequences of the transfer by netting, or to be able to detect fraudulent acts from the data itself. Obviously this training is necessary too in commercial law because many rules are affected by insolvency, and here I mean company law; credit law; law on property; law on securities; social law because of the effects of insolvency on unemployment; competition regulation; and sometimes international private law. Additionally, when judges are traders or managers, but not professional judges, as is the current system in French commercial courts, such judges need to be well trained in legal and procedural matters, for these issues are not within their basic experience. That is a lot. Nobody knows everything, so we have to look for ways or providing such training and making proceedings efficient.

How can we provide for or improve training of judges? First of all, training no longer means two or three years spent in a school of law, but takes place throughout a professional's life, it is a continuous ongoing education. One of the problems is whether such training should be mandatory or not. If it is not ongoing education, only those judges making the choice to go back to school would be well trained. Education is a right, but it is also a duty for judges their whole life long. And I believe several days in a year is not too much time to take for training updates for anybody involved in insolvency cases or in other related matters.

It is worse for civil judges, of course, when they are appointed by the states without any formal training as a lawyer for example. But I believe in this last case, lawyers are not necessarily familiar with insolvency matters, so that they too need education in such matters.

Another issue could be specialization of judges. It would mean that the civil judge could become acquainted with insolvency matters before they had to deal with such matters and thereafter they would spend a major part of his or her time within this scope. That is what specialization should mean. It does not mean that the judge only occasionally deals with such cases, but that he or she spends most of their time on those types of cases. It means too that the court should be big enough to deal with a significant number of proceedings; if you have to manage such cases only once or twice a year, you will probably lose time and make mistakes. It means also that the higher courts should include specialist judges. In this way, it would be possible to avoid the decisions of county courts being cancelled later because of the lack of expertise in the higher court. Exchanges of experience, between judges, practitioners, bankers, lawyers, and sometimes teachers too, could also be an aspect of training. But the focus should be upon exchange of information and experience among the judges themselves. Moreover information should be provided to the judges from several sources – from creditors, creditor committees, practitioners, experts – although judges have to be aware that information may be sometimes be nothing but lobbying. But this comment is not peculiar to insolvency matters. Of course, we could focus on procedural regulation and structure of the court itself. The court could provide the best conditions for training. I would like to mention at this point the judicial system in force in Belgium, where for 20 years insolvency cases have been dealt with by a specialized court chaired by a professional judge, assisted by 2 lay judges who are trained in a commercial field. They are chosen from among bankers, traders, company directors, retired managers and so on. A reform of commercial courts is being discussed in the French Parliament this month, with the intention of introducing such a system in the commercial court for insolvency cases. Germany had the same system, but only for commercial cases, not for insolvency proceedings. Insolvency proceedings in Germany are heard by judges of courts of summary jurisdiction and I have been told that German practitioners are not too confident with such professional judges. It should be noted, on this point, that in the German insolvency system, the main decisions are approved by creditors themselves or by creditors committees.

In conclusion, I would like to focus on 3 short very general proposals. States should provide material and legal conditions of independence to well-trained judges in order to allow judicial control wherever such control is deemed necessary. I do not include here voluntary and out-of-court agreements before insolvency, but the real judicial insolvency proceedings. The court should be structured to provide for experience in the area of insolvency, through exchanges among judges and a basic on-going education. Practitioners and judges should, as far as possible, get a common training to foster cooperation and to provide for the efficient conduct of insolvency proceedings. Thank you.

Ms. WEE

On the very first day during the interrogation, I said that the greatest need is training, training and training. But at that time, I did not really think that it would be much further discussed in this gathering, because I did not see the role of UNCITRAL really impacted by training. However, I have been proven wrong. Over the last two days, this gathering has strongly reaffirmed and restated over and over again that it is critical for an insolvency system to function. That can only happen if its professionals are trained (and by professional

I am including receivers, liquidators, administrators, trustees, whether public or private, etc.). As Lawrence Liu said, a strong message should emerge from this meeting that judges and professionals should be trained, and this panel of evaluators has deliberated on what exactly should be the role of UNCITRAL with respect to the training of professionals.

When we discussed a wishlist yesterday, guidelines and allocated resources to assist courts were on that list. It was also mentioned that official liquidators and receivers should have an implementation guide and system to assist them. Other suggestions from the floor included the establishment of training centres, the request that training should be coordinated to avoid unnecessary duplication and that resources should be appropriately channelled. There was even a suggestion that any work that came out of UNCITRAL should include a self-funding mechanism to ensure that training would be sustainable and continuous. The evaluators have struggled with this and we have concluded that the role of UNCITRAL with respect to the training of professionals should be to give a strong message and a strong nudge to policy makers and the insolvency community that it is not enough simply to have the laws in place, but that for the insolvency system to work, the training of professionals is an essential element. Some of the policy issues that should be included in any training material would be the very fundamental and basic purposes of insolvency law, whether it is a process of renewal or growth or whether it is merely an exit strategy. It should also include constant evaluation of the changing state of our world and other commercial economic and social laws and should not just focus on the substantive issues of insolvency. Thank you.

Role of regulators

Mr. GITLIN

One of the decisions that has to be made when constructing and modifying the bankruptcy system concerns whether regulators should play a role and, if so, what role? I found what happened in Mexico quite interesting. When they were thinking about their law, the Mexicans visited us in the US and we introduced them to the US Trustee System. They went back and concluded that part of the integrity process of their system should include a special Institute which happened to be part of the court system (in the US the trustee is not) and which is responsible for appointing all the officials (there are three levels of officials in Mexico) and for monitoring their quality and integrity on an ongoing basis. There are some jurisdictions that have courts and judges only for that role and some jurisdictions where the Official Receiver plays that role. So, one of the things that the UNCITRAL report should come to grips with as part of our roadmap for consideration is why people choose different alternatives, what are the policy and cost considerations.

Out of court restructuring

Justice FARLEY

As discussed earlier, it appears advantageous to have a system which, with a functional law and infrastructure, encourages the parties to avoid the delay of a formal court proceeding over any extended period of time. If the parties recognize the certainty of outcome in a functional system, then they may more efficiently negotiate in the shadow of that system a resolution either completely independent of that system or one which is effectively speedily dealt with by the court on a prepack basis.

Mr GITLIN

Everything we talked about today, and the projects we are defining out of this process, end up relating to how you help make a rescue happen. In the end when a deal is made we add value. It is very important as we approach both developed countries and developing countries to make sure, after we have done all our work, that we look and say: Have we put the elements in place that facilitate the making of a deal? Because if the answer to that is no, we have not accomplished what we have set out to do. In deal making, we all agree that one of the most complicated parts is to get the creditors to agree among themselves. We are now finding new creditors to deal with, they are not just banks, they are bondholders, they are secondary purchasers, they are derivative holders. There is a complexity of creditors that is growing even in medium-sized cases that require a fresh look. That is really why the INSOL Lenders Group took the London approach and, together with what has been done around the world, brought it up to date in the Principles. So the Principles that have been established for out-of-court negotiations, although they are called “out-of-court”, really set a framework for how to deal with the new complexity of deal making, with respect to the debtors, with respect to creditors among themselves and then creditors and debtors. If we were asking Justice Farley to issue a channelling injunction, I would request that one of the elements be that each of us take the Principles back to our banks, to our central banks, and try to get them familiar with the concepts, because as Terry Bond said so well yesterday, the quicker people get to the table, the quicker we have a deal. And these are rules as to how to get to the table.

The next question, as Justice Farley mentioned, is what happens if you cannot get 100% of the creditors to agree out-of-court. We need to look at our insolvency law project and ask what we must include in the law that allows you, if you have 75 % of the creditors agreeing out-of-court, to roll it into court very efficiently. We should ask the INSOL Lenders Group what they would like to see in the law to effectuate the work they have done on out-of-court and feed that back into the UNCITRAL process.

The third element to encourage deal making is to test the rescue law to make sure that the leverage is balanced between debtors and creditors in any insolvency law. Balanced leverage encourages deal making both in and out of court.

Timeframe

Justice FARLEY

Let me deal with timeframe, resources and stakeholder participation. As earlier indicated, we feel that this programme should, absent unusual complications, be completed in 2 years with an UNCITRAL Working Group developing a recommended comprehensive law with specifics and with variations addressing the important issues in insolvency to satisfy the circumstances and stages of development of each jurisdiction. A realistic best practices code and alternatives would be appropriate. The pros and cons and implications of these versions are important and necessary. We strongly recommend that the first meeting of the Working Group be convened in approximately 6 months to give sufficient time for draft consideration to be produced, examined and revised in context. Anything sooner would likely result in undue wheel spinning as this process works best when the Group has fairly well thought out positions and alternatives reduced to paper. Appropriately, the work will progress on a piece

meal basis with the Working Group addressing the priorities of how to deal with matters. The UNCITRAL staff will coordinate resource facilities including the organization of various expert groups in the interim. The preparation of the paper distributed this morning, "Issues regarding the potential development of guidelines for effective insolvency laws", put out by certain of our American participants, is an example of a helpful resource paper for consideration. We know that the rest of you and other interested persons will have similar input for resource material including analysis of critical aspects of your own present regime. We would encourage you to provide the UNCITRAL staff with such as soon as possible: what works and does not work and why?

It is recommended that the July 2001 INSOL/UNCITRAL Judicial Colloquium be devoted to obtaining the views of the diverse judiciary attending as to the judicial elements in this programme for consideration by the Working Group. To ensure that the Working Group has appropriate depth and balance, we recommend that its composition include representation by all stakeholders on a world-wide basis including the general different legal systems and including representatives of legal, accounting and other insolvency practitioners, turn-around managers, the judiciary, regulators, (historical and transferable debt) lenders and the business community/debtor surrogates. This is not a static project once the initial work is done. There will have to be completion of the items not addressed on the initial piecemeal basis. As well, there should be periodic reviews and updates as business practices and insolvency requirements and responses evolve.

Finally, each of us should take back to our own jurisdictions the desirability of implementing the UNCITRAL Model Law on Cross-Border Insolvency and make effective representations aimed at having it enacted sooner rather than later without waiting to see what others do. Judges may most effectively acknowledge in an appropriate decision or otherwise note that it contains a helpful set of principles to guide the court.

The end result objective of this UNCITRAL initiative is that we have a blueprint with options for suitable insolvency law to fit our individual jurisdictions needs. That, together with the necessary infrastructure support, will give each jurisdiction a standard against which the essential participants will be able to measure achievement of a functioning insolvency system, whether we be in an established or developing economy. The evaluation team would like to commend all participants for their thoughtful and thought-provoking participation. Thank you.

KEY ELEMENTS FOR A DRAFT LEGISLATIVE GUIDE

1. Eligibility criteria
2. Access criteria for liquidation and rehabilitation
3. The bankruptcy estate
4. Automatic stay
5. Role of management
6. Role of creditors' committee
7. Treatment of contractual obligations
8. Avoidance actions
9. Distribution priorities
10. Additional issues specific to rehabilitation cases:
 - a. Relationship between liquidation and rehabilitation
 - b. Business operations and financing
 - c. Provisions relating to rehabilitation plans
11. Guidelines for voluntary out-of-court restructuring