

Indonesia

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Formal insolvency proceedings and restructurings are relatively recent developments in Indonesia.

As part of the general continuation of the application of Netherlands-Indies legislation, Indonesia inherited the Bankruptcy Ordinance, first enacted in 1906. After independence, use of the Bankruptcy Ordinance declined rapidly and it was never amended.

In response to the need for more effective bankruptcy legislation to address the then-existing economic crisis, in 1998 the Indonesian government amended the Bankruptcy Ordinance by enacting Law 4/1998 (the Bankruptcy Law). The Jakarta Initiative Task Force (JITF), the Financial Sector Policy Committee and the Oversight Committee were also established in 1998 to facilitate corporate restructuring outside bankruptcy. These institutions are no longer in existence, but made noteworthy achievements during their tenure.

Other issues affecting bankruptcy and restructuring in Indonesia include the non-confrontational nature of Indonesian business customs and perceived difficulties in the administration of justice. The Asian Development Bank, the World Bank, the International Monetary Fund and others have commented extensively on the latter issue. Revisions to remove ambiguities and correct fundamental problems were enacted in 2004 as Law 37/2004 (the New Bankruptcy Law).

I Legal framework and the effectiveness of court processes/legal remedies

1.1 Describe the nature and effectiveness of the following:

(a) Debt recovery remedies where the creditor has no security

The enforcement of private unsecured debt commences with the filing of a claim with the district court of the place where the debtor has its usual place of abode, unless otherwise agreed. However, any district court judgment is subject to appeal through the court of appeals and cassation procedures before the Supreme Court; thereafter, there may be a civil review before a different chamber of the Supreme Court. Pending appeal, no order can be enforced. Consequently, obtaining an enforceable order can be a lengthy and expensive process.

An unsecured creditor can also petition for the debtor's bankruptcy in the Commercial Court, the procedure and consequences of which are considered in section 1.1(d).

(b) The enforcement of security

Security over assets in Indonesia is generally taken and enforced as follows:

- A mortgage can be taken over immovable property. In principle, a

mortgage holder has a right of direct execution without a writ of execution, but in practice a court order is likely to be required.

- A fiduciary transfer of ownership for security purposes can be taken on movable property and untitled land. To obtain possession of goods subject to a fiduciary transfer, the creditor must institute legal proceedings unless the debtor cooperates voluntarily.
- A pledge can be taken over movable property. A pledge requires the pledged property to be brought outside of the debtor's possession and repossession of the pledged property is normally less problematic.
- A fiduciary assignment for security purposes can be taken over intangible property. To enforce a fiduciary assignment of receivables, each obligor must be notified to pay the assignee, and a creditor's only recourse against an obligor or debtor that disregards such notification is to institute legal proceedings.

In principle, creditors can enforce security through a sale by public auction without recourse to the courts. In practice, however, this is difficult. All realisations by secured creditors (except assets subject to fiduciary assignments) must be through sale by public auction, unless the debtor voluntarily consents to another sale mechanism. All public auctions must be notified to and supervised by the State Auction Office (SAO), and may be conducted by either the SAO or a private auction house. The SAO is frequently criticised for a lack of transparency and invariably requires a court order for the auction, unless the debtor voluntarily consents to the sale. Auction fees total:

- 12 per cent of the proceeds of sale for movable property;
- six per cent for immovable property; and
- 1.5 per cent and 0.375 per cent respectively if the assets are not sold.

A further difficulty is that registers of mortgages and other security interests are kept manually and held regionally. It is thus difficult for lenders to confirm that debtors have not previously granted security over the same collateral. The security interest registered first will generally have priority.

Court proceedings to foreclose on secured assets are substantially the same as for the enforcement of unsecured debt (see section 1.1(a)), with the attendant disadvantages.

(c) Corporate bankruptcy/liquidation processes

Under the Bankruptcy Law, one or more creditors may file for the debtor's bankruptcy if:

- the debtor has at least two creditors; and
- the debtor has failed to pay at least one of its debts which have become due and payable.

A bankruptcy petition may also be filed by the debtor itself or, if the public interest so requires, the public prosecutor. Special rules apply to banks, security houses and insurance and reinsurance companies, and state-owned companies engaged in public interest business (see section 1.2(d)).

In reality, the Commercial Court has not interpreted the bankruptcy test consistently thus far. Some examples of its decisions to date include the following:

- not recognising that the debt was due and payable when the loan had been accelerated because the final repayment date had not occurred;
- not recognising debt under a swap transaction as a valid debt for these purposes;
- disallowing an unpaid claim for damages as the basis of a bankruptcy filing;
- not recognising as creditors (foreign) holders of bonds sold through the market; and
- not differentiating partial restructurings which result in disparate treatment between lenders.

One reason for the enactment of the New Bankruptcy Law was to give precise interpretations of certain provisions under the Bankruptcy Law.

(d) Formal corporate rescue processes

Only one formal corporate rescue process is available: a suspension of payments (moratorium) under Chapter II of the Bankruptcy Law. During this suspension the debtor is excused from making payments to its unsecured creditors and secured creditors cannot enforce their security without the court's consent.

The purpose of a suspension of payments is to enable the debtor to propose a composition plan. A plan can also be proposed by a receiver appointed during bankruptcy proceedings.

If the debtor petitions for a suspension of payments, the Commercial Court must grant a provisional moratorium and appoint a supervisory judge and an administrator to assist the debtor in managing its estate. The debtor will be entitled to manage and dispose of its assets jointly with the

administrator.

The Commercial Court must call a meeting of unsecured and secured creditors within 45 days of granting a provisional moratorium. At this meeting, unsecured creditors and secured creditors may either:

- approve a composition plan, if the debtor has submitted a plan to the court; or
- agree to convert the provisional moratorium into a permanent moratorium of a maximum of 270 days from commencement of the provisional moratorium. The permanent moratorium is extendable if the creditors and the court consent.

Any creditors' meeting to consider the plan must be held before the permanent moratorium expires.

Decisions require affirmative votes of more than 50 per cent in number and 66.67 per cent in value of the unsecured creditors present or represented at the meeting, and more than 50 per cent in number and 66.67 per cent in value of the secured creditors present or represented at the meeting. If no plan is submitted and the unsecured creditors fail to extend the moratorium, the court will declare the debtor bankrupt. If the creditors approve the plan, the Commercial Court must hear an application to ratify the plan and will hear dissenting creditors. The Commercial Court must refuse to ratify the plan if:

- the value of the debtor's assets considerably exceeds the amount agreed in the plan;
- performance of the plan is insufficiently assured; or
- the plan was concluded as a result of fraudulent transactions or undue preference of one or more creditors, or other unfair means, regardless of whether the debtor or any other party cooperated to this effect.

Once ratified, the plan becomes final and binding on all creditors, except dissenting secured creditors, which are entitled to compensation from the debtor at the lowest of either the value of the security or the amount of the outstanding secured claims. There are no implementing regulations as to how this recent change for dissenting secured creditors will work and no precedent set.

A plan can be submitted only once; if it is rejected by the unsecured creditors or not ratified by the court, a bankruptcy declaration will be made and the debtor's assets will be liquidated. If a plan submitted by a bankrupt debtor is not approved or

ratified, a 'state of insolvency' will be triggered (see section 1.2). In practice, however, the receiver may call for meetings between the lenders and the debtor prior to the final vote in order to negotiate the terms of the plan.

Following ratification of a plan, the suspension of payments or bankruptcy proceedings and the appointment of the administrator or receiver (as applicable) will be discharged. The business and assets of the debtor will be returned to the debtor's control, subject to any specific provisions contained in the plan.

(e) Informal corporate rescue processes

Given the enforcement difficulties highlighted above, the preferred route of creditors is negotiation on a private basis with cooperative debtors. The more prominent international accounting firms, international and domestic law firms and investment banking advisers have frequently advised on, documented and generally assisted and supported these private processes.

To facilitate private restructuring negotiations, the JITE, the Financial Sector Policy Committee and the Oversight Committee were established in 1998. The JITE mediated in debt restructuring negotiations among Indonesian debtors and their creditors, using the London Approach, and gave tax concessions to debt restructured under it. It closed in December 2003 as the government considered its work largely complete by then.

1.2 What are the formal processes to effect a liquidation of the company's assets?

A distinction is made between a voluntary liquidation by shareholders governed by the provisions of the Company Law and a forced liquidation initiated by creditors.

A forced liquidation takes place under the Bankruptcy Law. It is triggered by a state of insolvency, which occurs when, after all claims have been submitted, no plan has been proposed by the debtor, or a proposed plan has been rejected by creditors or has failed to be ratified by the court, as described in section 1.1(d).

In a forced liquidation, the receiver will liquidate the debtor's assets under the supervision of the supervisory judge. The proceeds will be distributed among the creditors in accordance with the priority of their respective claims (see section 7.2). Receivers must hold a licence to act as such.

1.3 What is the effect on debt collection and the enforcement of security of:

(a) An adjudication of corporate bankruptcy/liquidation?

Unsecured creditors may not enforce due debts other than by claiming in the bankruptcy procedure.

Secured creditors' rights to enforce their security are automatically stayed for up to 90 days following a bankruptcy declaration, although the court may lift or vary the stay. If a secured creditor fails to enforce its security within two months of the date on which the company enters a state of insolvency, it will be required to deliver the security to the receiver for enforcement and, as a result thereof, will be liable to share in the bankruptcy costs. In practice, this would be difficult to achieve.

(b) The commencement of a formal corporate rescue process?

See section 1.1(d).

(c) The initiation of an informal corporate rescue process?

In theory, creditors remain entitled to exercise their legal remedies against a debtor when informal restructuring or rescheduling negotiations are in progress. However, there is a presumption in law that negotiations will be in good faith. The court is likely to refuse enforcement while negotiations continue and a 'cooling-off' period of several weeks is recommended after negotiations have irretrievably broken down, to reduce the risk of the court refusing enforcement.

The JITF facilitated the restructuring of 102 companies with distressed debts totalling US\$26.91 billion. After the closure of the JITF, some members of the JITF founded the Indonesian National Mediation Centre for the purpose of facilitating and mediating commercial and other disputes.

(d) The initiation of an insolvency or insolvency-related process under any special legislation?

If the debtor is a bank, only Bank Indonesia (the central bank) may file the bankruptcy petition.

If the debtor is a security house, only BAPEPAM (the Capital Markets Supervisory Board) may file the bankruptcy petition.

If the debtor is an insurance or reinsurance company, a pension fund or a state company

engaged in public interest business, only the minister of finance may file the bankruptcy petition

A bankruptcy petition may also be filed by the debtor itself or, if public interest so requires, by the public prosecutor.

1.4 Are insolvency procedures involving a corporation incorporated in your jurisdiction recognised if they are started in another jurisdiction?

Only three sections in the Bankruptcy Law deal with cross-border aspects of bankruptcy, and unfortunately these provisions are not very clear.

Based on writings and case law developed in the Netherlands, it may be assumed that Indonesian law adopts the principle of territorial effectiveness of bankruptcy. This principle entails that any insolvency judgment or ruling on insolvency by a foreign court will have no effect on assets situated in Indonesia. The fact that any such foreign judgment has been pronounced does not limit the right of other creditors to foreclose on assets in Indonesia.

The above does not mean that no recognition at all is given to a foreign insolvency judgment. For instance, a receiver appointed by a foreign court in bankruptcy proceedings outside of Indonesia will likely be recognised in Indonesia. However, certain practical difficulties stem from the Bankruptcy Law; these are outlined in section 2.

1.5 In what circumstances would the directors or officers of a company in financial difficulties face potential personal liability for continuing to trade? In practice, are any such provisions actually enforced?

If a company has been declared bankrupt and its assets are insufficient to cover its losses, each director is jointly and severally liable for losses caused by the fault or negligence of the board of directors.

Directors who can establish that the losses were not due to their individual fault or negligence will not be held liable.

Shareholders representing at least 10 per cent of the issued share capital may issue proceedings against the directors in respect of such losses. In practice, legal actions of this nature are rare.

2. What are the advantages and disadvantages of triggering a formal procedure?

There are relatively few advantages to be gained by creditors through triggering a formal insolvency or debt restructuring procedure. In some circumstances, there are considerable risks in doing so and bankruptcy procedures can be turned against creditors.

There have been few major bankruptcy cases.

Many creditors have sought bankruptcy declarations against uncooperative debtors, but often the debtor has been able to frustrate the process.

Formal insolvencies of small and medium-sized enterprises are not uncommon, although for cultural reasons they are below the rate commonly seen in other jurisdictions. In practice, however, it is extremely difficult for creditors (particularly foreign creditors) to trigger or subsequently proceed with formal insolvency proceedings against a debtor that is associated with a major Indonesian conglomerate without the consent of the debtor and its majority shareholders.

This is consistent with the Indonesian cultural preference for negotiation and face saving. It is considered inappropriate for a creditor to resort to court proceedings. What might be achievable through a negotiated settlement becomes unattainable if the approach taken is apparently hostile to the interests of management and majority shareholders. This may remain true even if negotiation has failed after considerable efforts and a long period of time.

Practical difficulties encountered in relation to the Bankruptcy Law (and Indonesian laws in general) include the following:

- Certain provisions – particularly on procedural matters – are unclear and/or are applied inconsistently. Legal rules about the substance of conflicts are not ignored, but are regarded as providing the bounds within which there is considerable room for negotiation of the least damaging compromise – and the one that allows for the most face saving.
- When the Bankruptcy Law was enacted in 1998, considerable effort was made in selecting and training judges for the Commercial Court. However, seven years on, the results have generally been disappointing. In many cases, particularly in more complex matters such as derivative transactions, claims appear to have been misinterpreted. There have been cases where additional previously unknown creditors have been allowed to appear, to vote

and to receive distributions.

- The power of judges to interpret the law has traditionally been used very broadly and judges often adjudicate matters in a broad based, inquisitorial manner. The logical link between the facts of the case and the documents submitted and the court's findings has often not been immediately clear. Only recently have judges begun to write carefully reasoned conclusions to support their decisions.
- There is no system of precedents under which the courts are bound by earlier decisions of higher courts, and decisions are readily overturned for reasons often not immediately obvious from the factual findings. One effect is that a receiver or administrator appointed by the Commercial Court has uncertain tenure and is often reluctant to act until all appeals have been exhausted.
- There is no public access to information regarding the value of the debtor's assets and its liabilities. Information provided by the court is limited to the decision made, the date of the decision and the case number.
- The official income of judges is low by the standards of local professionals. Receivers and administrators are statutorily remunerated based on realisations.

Uncertainties and difficulties in enforcing security rights are described in section 1.1(b).

3. What are the practical options for out-of-court restructuring?

The only practical option for out-of-court restructuring is to negotiate, which generally requires considerable patience, relationship building and consensus building, and sustained efforts to seek out win-win opportunities. In practice, litigation is not a viable option, unless the debtor has substantial business interests and assets outside Indonesia which can be attached by creditors through the courts of the jurisdiction in which the assets are located.

Most of the usual forms of debt restructuring have been used in Indonesia, including debt rescheduling, conversion of debt into convertible notes, conversion of debt into equity, debt refinancing, debt buyback and cancellation of debt ('haircuts'), although haircuts are less common. Interest holidays and reduced interest rates are common.

The suspension of payments mechanism is sometimes used to make an out-of-court restructuring which is agreeable to a majority of creditors binding on all creditors, including dissenting minorities, by means of a pre-packaged composition plan.

The name of the game remains 'settle and sell': negotiate a restructuring agreement and exit through a sale of the debt. Debt traders can be active, and direct and indirect debt buybacks by debtors and their shareholders are common. Business performance improvements tend to follow restructuring agreements and sales of debt.

The negotiation of the best deal possible in a reasonable timeframe requires considerable commitment of time and effort to build the necessary consensus. A significant part of the process relies on personal relationships with key shareholders and executives of the debtor.

The extent to which the debtor requires further funding can influence the degree of cooperation. Threats of litigation are not realistic or helpful. Creditors have found that encouraging the debtor to use a reputable financial adviser can assist in bridging the gaps.

There are exceptions to the above, particularly among corporate groups that do not have a majority shareholder or that have a major foreign shareholder and links to the international business community.

4. What is the effect on the management of a company of:

4.1 An adjudication of corporate bankruptcy/liquidation?

The debtor and its directors lose the right to manage and dispose of its assets in the event of bankruptcy or liquidation. In a bankruptcy, a receiver is appointed to represent the debtor.

4.2 The commencement of a formal corporate rescue process?

Once a suspension of payments has been granted, the board of directors retains its powers to manage and dispose of the debtor's assets, but can only exercise such powers jointly with the appointed administrator(s).

4.3 The initiation of an informal corporate rescue process?

During rescheduling and restructuring negotiations, the board of directors retains full management control of the debtor. However, creditors often require, in consideration of temporarily suspending their enforcement rights, the establishment of monitoring arrangements, cash-flow escrow arrangements and creditor approval for material expenditures, new indebtedness, payment of dividends and/or the creation of security over assets.

Enforcement of such requirements may be difficult in the absence of effective judicial sanctions.

4.4 The initiation of an insolvency or insolvency-related process under any special legislation?

The transfer of management duties and powers to a receiver may be granted by an interim order of the Commercial Court immediately after a bankruptcy petition has been filed if the danger of embezzlement can be proven.

5. Roles of key players involved in the restructuring and insolvency process

5.1 Who is responsible for the 'case management' control and administration of a corporate bankruptcy/liquidation, a formal rescue or an informal rescue?

The receiver is responsible for administration and control of the bankruptcy. The supervisory judge oversees the performance of the receiver's duties and his approval is required for certain material transactions, such as termination of contracts and sales of assets. The supervisory judge also hears petitions from the creditors and the debtor relating to the receiver's actions.

The Commercial Court may appoint a formal creditors' committee to advise the receiver. If the receiver does not follow the committee's recommendation, the committee may appeal to the supervisory judge.

In addition, a creditors' meeting must be convened when so requested by at least five unsecured creditors representing at least 20 per cent of the total unsecured claims admitted.

In practice, creditors' committees will generally be informal in order to facilitate more effective and efficient negotiations, and to avoid any liability

issues which may arise from involvement in formal committees.

5.2 Who is responsible for the ‘case management’ control and administration of a case of corporate insolvency under any special legislation?

No special legislation applies.

5.3 Who is responsible for preparing the restructuring plan in a formal or informal rescue?

In bankruptcy procedures, the debtor and the appointed receiver are responsible for preparing the composition plan. In a suspension of payments, this duty falls to the debtor alone, but the plan can also be prepared with the appointed administrator(s). In both cases a creditors’ committee may render advice and assistance, either formally or informally. As mentioned, input from creditors can be given at creditors’ meetings and subsequent iterations of draft plans issued. This can be a moving target when creditors’ claims have not been finalised.

In a private restructuring, it is generally the debtor’s responsibility to prepare the restructuring plan (which may take the form of a plan to be proposed in a suspension of payments), although it is open to the parties to make alternative arrangements such as through engaging independent financial advisers.

5.4 Who is responsible for preparing the restructuring plan in a case of corporate insolvency under any special legislation?

No special legislation applies.

6. What financial information is available to creditors in a corporate bankruptcy/liquidation, a formal rescue and an informal rescue?

Financial information is limited. Publicly listed companies are required to publish quarterly accounts, but these are often lodged late as the penalties are insignificant. These accounts are intended to protect the interests of minority shareholders. Banks and insurance companies must publish accounts. All companies with total assets greater than Rp25 billion (approximately US\$2.5 million) are required to submit audited accounts to the company registrar under the Ministry of Trade. In practice, there is less than full compliance and

access to such information is limited.

In a bankruptcy or liquidation, the information to be made available to creditors is not specified and is, in practice, extremely limited. Assets and liabilities will be identified and valued by the receiver, who reports to and is supervised by the court, not the creditors.

Creditors’ claims are verified in a verification meeting, in which creditors are permitted to view, verify and object to claims submitted. In the verification meeting(s) the receiver (and not creditors generally) decides whether to allow or reject each claim, and determines the value and priority (if any) of allowed claims, also drawing on information from the debtor. In larger bankruptcies with multiple creditors, this process may occur over many meetings.

Information regarding the quantum, type of debt and verification status is generally not available during this process.

If the receiver and a creditor whose claim is challenged cannot agree, special proceedings will take place to determine whether the claim should be accepted. This notwithstanding, there have been cases in which previously unknown creditors have been allowed to appear, vote and receive distributions despite objections from other creditors.

In case of liquidation, once the list of admitted claims has been agreed and all realisable assets have been liquidated, the receiver will prepare a distribution plan for approval by the supervisory judge. Where the plan envisages a going concern, in practice there will be little by way of immediate realisation. If approved, the distribution plan is filed with the Commercial Court and may be examined by creditors.

Creditors may oppose the distribution plan in a Commercial Court hearing at which both the receiver and creditors may be heard. The court may either confirm the distribution plan with or without amendment, or reject it.

In a suspension of payments, the above procedure by and large applies.

In an informal restructuring, the financial information available varies greatly, depending on the extent to which the debtor wishes to cooperate and to conclude a restructuring agreement quickly. It is often difficult for creditors to obtain an accurate picture of the debtor’s financial position, causes of failure and ability to pay. Creditors sometimes appoint an independent financial adviser to review and report on the debtor’s financial position and prospects.

The debtor will produce financial projections and will sometimes agree to allow the creditors' financial adviser to review its projections. However, this is generally of more limited value than in other jurisdictions and the situation is not made easier by the volatility of the Indonesian rupiah. Specific problems encountered frequently include the following:

- The projections are prepared specifically for creditors and do not reflect management's real view of prospects;
- The projections lack integrity and may not link to actual historical performance and published financial statements; or
- There is a lack of information to support the financial data and detailed assumptions made.

Creditors often seek the debtor's consent to the monitoring of its cash flow and performance after the restructuring.

7. Financial issues

7.1 What are the main areas from which funding is generally utilised by companies undertaking either formal or informal restructuring?

In a suspension of payments, with the approval of the administrator, a debtor is entitled to borrow new funds and can provide security for such financing. This security will rank behind the existing security (if any) on the same assets, but the new lending is not subject to the moratorium and must be repaid in full when it falls due.

Outside of the suspension of payments regime, new loans extended to debtors in relation to corporate restructuring are not regulated and do not have automatic super-priority over administrative expenses and other preferential claims; however, they may be rewarded by equity carve-outs.

In an informal restructuring, it is unusual during negotiations for additional funding to be made available by either existing or new lenders, because of the lack of certainty over whether new lending will be afforded priority in the restructuring. During the negotiation period, it is common for debtors to withhold payments of principal while sometimes continuing to pay interest. As a result, if this period is protracted, there is often a significant build-up of cash.

Unusually, on or after completion of the restructuring agreement, some existing creditors may provide additional finance if the restructuring

agreement gives this priority over existing debt. Administrative expenses and other preferential claims continue to have priority as a matter of law.

More commonly, new lenders (almost exclusively Indonesian banks) provide additional funding on or after completion of the restructuring, and are afforded priority or security. The new debt will generally be used for a combination of:

- working capital finance;
- capital expenditure;
- repayment of existing debt; and
- the buying out of existing debt.

From 1997 to 2003, Indonesian banks virtually stopped corporate lending and focused more on readily securable and enforceable commercial and consumer lending. There was also a period of consolidation within the banking sector during this period. In response to increasing stability and a more positive outlook, the main indicator Bank Indonesia Certificate (SBI) borrowing rate fell below 10 per cent and Indonesian banks are increasingly looking to commercial lending to maintain their net interest margin. However, in mid-2005 the economy was hit by an increase in the crude oil price and a fall in the rupiah exchange rate. These factors forced Bank Indonesia to increase the SBI rate to 10 per cent.

The shortage of quality lending opportunities and difficulties in recovering debt from major corporates have not eased, and the risk of default remains high, but Indonesian banks are becoming less risk averse and refinance lending to companies that have restructured their debts is increasing.

Foreign banks in Indonesia generally continue to restrict new commercial lending to a limited range of industries (especially those with export opportunities), to affiliates and subsidiaries of foreign companies, and to Indonesian companies with major overseas operations.

New loans are not regulated and, except in formal bankruptcy and suspensions of payments procedures, do not have automatic super-priority over administrative expenses and other preferential claims.

7.2 In what order are creditors paid in a corporate bankruptcy/liquidation?

Secured creditors are paid from the sale proceeds of assets subject to their security (after payment of auction costs). If the proceeds are insufficient to pay the secured claims in full, they are entitled to claim the balance as unsecured creditors. If there is a

surplus, this becomes available to unsecured creditors and will be distributed as described below, together with all realisations from assets not subject to security:

- The costs of the bankruptcy (including court and auction costs), employees' wages and the receiver's fees have priority over all other unsecured debts. The court may make an enforcement order for payment of costs of the bankruptcy and the receiver's fee.
- Funds available after payment of the costs of bankruptcy are available for, first, privileged creditors such as the state in respect of taxes and, second, unsecured creditors.
- The preferential order of claims is set out in a number of laws and regulations which are detailed and complex, and are not always interpreted consistently.

7.3 Are there any legal provisions that might operate to invalidate the creation of security, the disposal of an asset or the payment of a creditor by a company in financial difficulties?

Pre-bankruptcy transactions favouring one creditor over others can be annulled if:

- the transaction qualifies as a legal act, was voluntarily undertaken (ie, without contractual obligation) and has had a detrimental effect on the creditors; and
- the parties to the transaction knew or should have known that the transaction was prejudicial to other creditors.

There is a statutory presumption that such knowledge existed if the transaction took place in the year prior to the declaration of bankruptcy and:

- was under value;
- granted security for debts which had not yet fallen due; or
- was concluded with certain related parties.

A transaction which the debtor was contractually obligated to perform (eg, payment of a debt due and payable) may be annulled if it is shown either that the creditor knew that a bankruptcy petition was pending or that the transaction was the result of collusion between the debtor and the creditor.

The same test for invalidating antecedent transactions applies in informal restructuring procedures, but there is no presumption of knowledge of prejudice.

7.4 What is the position of both unsecured and secured creditors that vote against, do not agree with or do not consent to either a formal or an informal rescue plan?

Secured creditors and creditors with a statutory preference or priority cannot be bound by a formal or informal rescue plan. However, all unsecured creditors in bankruptcy proceedings, and all creditors – except dissenting secured creditors – in a suspension of payments, will be bound by a plan if it is approved by the requisite majorities of creditors and is ratified by the court, as described in section 1.1(d).

Creditors cannot be bound by an informal rescue plan without their individual consent. To avoid this problem, many informal rescue plans are negotiated out of court and then ratified as plans through the suspension of payments procedure.

Secured creditors can change class to become voting creditors if they annul their security rights prior to the verification of claims. Theoretically, a partial change of class is permissible, subject to a third-party valuation of the underlying security.

7.5 What actions can creditors take if they are not satisfied with the conduct of either a formal rescue procedure or a corporate bankruptcy/liquidation?

If a formal creditors' committee has been set up in either a suspension of payments or a bankruptcy, and the receiver or administrator does not follow the committee's recommendation, the committee may appeal to the supervisory judge.

Court decisions to allow or reject creditors' claims in a bankruptcy or a suspension of payments, and regarding the value and priority of claims that are allowed, are not subject to appeal.

A composition plan proposed in either a suspension of payments or a bankruptcy is subject to ratification by the Commercial Court. As mentioned in section 5.3, creditors and informal committees may seek to negotiate improved terms prior to voting on the plan. Creditors can be heard in the Commercial Court during the proceedings to ratify a plan. The court can refuse to ratify a plan on the grounds set out in section 1.1(d). The decision of the Commercial Court to ratify or reject a plan is subject to appeal in cassation proceedings before the Supreme Court.

Once ratified, a plan becomes final and binding. If creditors are dissatisfied with the debtor's implementation of the plan, they must seek nullification of the composition, which will result in bankruptcy if approved by the court; or

alternatively commence proceedings in the district court in the same way as they would for any other debt, or enforce any security held in the ordinary way, unless the plan contains special provisions permitting other remedies.

8. General

8.1 Can the insolvency regime be described as systematic and efficient for:

(a) The liquidation of businesses incapable of being restructured?

The insolvency regime cannot be described as systematic and efficient, due to the lack of transparency regarding the debtor's assets and liabilities and the practical requirement to auction secured assets, often with the participation of selected bidders only.

(b) The restructuring of debt?

In the sense that formal procedures do not necessarily pose a perceived threat to debtors, there is little real alternative, so restructurings are often stop/start processes. The real need for additional funding is the best incentive available.

8.2 What are the biggest legal and non-legal impediments to the systematic and efficient liquidation of businesses and restructuring of debt?

Cooperation of the debtor and reaching agreement between creditors.

8.3 Has the insolvency regime has been reformed in the last two years?

If so:

(a) What are the reforms?

The New Bankruptcy Law closed loopholes and clarified many points which could be misinterpreted. Some of the key changes were as follows:

- 'Debt' is now defined.
- The definition of 'creditors' now includes both secured creditors and preferred creditors that can file a bankruptcy petition without a loss of rights.
- Both unsecured and secured creditors must approve the plan proposed by a debtor under a suspension of payments (50 per cent in number and 66.67 per cent in value of those creditors

present or represented at the meeting).

- Only the Ministry of Finance may file a bankruptcy petition for insurance companies.

(b) Are the reforms being implemented so as to facilitate the systematic and efficient handling of corporate insolvency cases?

This is difficult to answer, as there have been few cases to date, but the reforms are viewed as progressive. Due to certain issues such as practical considerations in enforcing security, the regime is still debtor friendly, on balance.

8.4 Are there any other legal or non-legal changes in the last two years that have impacted on the operation of the insolvency law regime?

The Corruption Eradication Commission is slowly starting to gain momentum, which in turn is turning up the heat on the judiciary. This comes against wider calls and promises for increased legal certainty. The need for foreign lending for infrastructure and recovery from the 2004 tsunami has also increased the pressure for legal reform.

Most major restructurings have been completed, although there is now a wave of increases in non-performing loans. The attorney general is also looking into lending practices at certain banks. These wider issues may influence the operation of the formal process. A recent large bankruptcy case was viewed by many as being handled with considerably greater transparency than previous cases.

8.5 Is statistical information on insolvency cases and corporate insolvency published? If so, how? Is it easily and freely accessible?

No published data is available.

8.6 What is the most urgent reform required to facilitate the systematic and efficient handling of corporate insolvency cases (formal and informal)?

Specific reforms which would improve the existing regime, within a wider framework of legal certainty, transparency and corruption eradication, include the following:

- the filing of annual accounts and the availability of access to this information;
- an ability to enforce security directly; and
- the creation of centralised national land registries.