

SECTION R - INTER-RELATIONSHIP BETWEEN LENDERS AND BORROWERS IN CONTEXT OF FINANCIAL DIFFICULTY/INSOLVENCY OF THE BORROWER

Annexed to this working guide is a copy of a recent initiative launched in Indonesia to encourage private sector restructuring. In effect, this initiative proposes an informal (out of court) “work out” style of corporate restructuring in appropriate cases. We do not put this forward as a perfect model but it provides a good basis for examining the prospect of the possible application of a similar scheme or model in the countries which are the subject of this project.

Thus, in this section we ask that you read the annexure [particularly the part headed “1. Adoption of Principles”, paragraphs “a” to “i”] and, having considered those principles, comment on their possible application and implementation in your economy. In particular we would like to know the following:

- (a) by reference to each of the above paragraphs, comment on the suitability of their application in your economy;*

By and large, the principles of the Jakarta Initiative are applicable to Thailand. Specifically, with reference to 1(a)-(i) as numbered:

- (a) As normative conditions, these principles are applicable except in (3) with respect to the costs of the committee being borne by the debtor. This may be impractical administratively and unduly time consuming with negotiations over cost ceilings, vetting of costs etc., in circumstances where payment of such costs will in any case result in the reduction of the amount for payment to creditors by a correlated amount. Payment of costs by the debtor and with the knowledge that costs will be “pooled”, there is little direct incentive for creditors to minimize such costs, as opposed to when the creditors bear these costs themselves. Where there are a large number of creditors, this will especially be a problem.
- (b) We consider the involvement of senior managers is critical to the success of a financial restructuring.
- (c) Points 1, 2 and 4 are possible within the legal framework, but item 3

(subordination of creditors' claims to new creditors after standstill) is only possible if an Article 90 bankruptcy petition is filed with the court. For out-of-court work-outs, Article 94(2) of the Bankruptcy Act provides that creditors who provide funds knowing that the debtor is insolvent, shall not be entitled to receive payment in a bankruptcy case.

- (d) As normative standards, these points are legally possible and we would support such disclosure to facilitate informed decisions. However, detailed, comprehensive and accurate information is not always forthcoming. Confidentiality agreements may be breached often without clear evidence of breach to take recourse against the breaching party.
- (e) While it is most common for the company to produce a restructuring plan, production thereof should not be limited to the company. While the company may understand its operations and requirements more intimately than other independent sources, insolvency has arisen. In short, it may not know what is best for it, or have the expertise needed to restructure.
- (f) We agree this should happen, but in Thailand, "full and ongoing access" is unlikely to occur, especially where competing investors with alternative plans may be attempting to 'lobby' creditors. The debtor may perceive that information disclosed may be used against it if the information falls into the wrong hands, which may easily happen in spite of confidentiality agreements. If such doubts exist, the tendency is to withhold information.
- (g) Again, we would agree with these points. There may be considerable differences in the logistics of arriving at a restructuring proposal between debtors, depending on the particular circumstances.
- (h) A "pre-negotiated" plan between creditors is not specifically recognised under Article 90 of the Bankruptcy Act, although the practice of entering into such a plan before proceeding to court is now apparent in Thailand. A contractual relationship will exist between parties that have entered into a pre-negotiated plan (usually including debtor, investor and consenting creditors), with contractual remedies available for breach. However, the court will consider the plan in terms of the legislative criteria under Article 90, not what the parties have contractually agreed upon. Recourse to the courts is necessary, where creditor support representing 75% of the debt is

required, if the plan involves the injection of new capital to avoid the effect of Article 94(2) [see s.R(c)].

- (i) Substantively there should be no discrimination between domestic and foreign creditors, although procedurally (time limits, etc.) there needs to be some differentiation. This is the case with the current Thai law.
- (b) *state the difficulties that might be encountered in their application in your economy;*

Point a.(3) is possible, but impractical. For point c.(3), new funds will be prejudiced against unless an Article 90 application is made. Hence, this is something of a constraint on out of court work-outs involving new funds. Full and frank disclosure of information is not the norm in Thailand. Confidentiality agreements are common, but are also commonly breached. Nonetheless, such prior agreements may contractually restrict disclosure of the information stated in d., in addition to the general reluctance to disclose sensitive information.

- (c) *briefly state whether and what changes or additions might be required to the law in your economy for the application of the “work out” methodology and whether such changes or additions are a practical possibility.*

The main legislative change would be to amend Article 94(2) to enable creditors to inject new funds into an insolvent debtor without being prejudiced against, i.e. allowing them to claim against the debtor. The Bankruptcy Act could also be amended so as to specifically recognise “pre-negotiated” work-outs as agreed between a requisite number of creditors, debtor and investor(s), as the case may be.

Finally, in this section, we would like to know your opinion generally on this initiative, the areas that you regard as strengths; areas that are weak; and areas where you consider modification and improvement might be made.

Generally, we consider the Jakarta Initiative to be a useful guide. The principle that the debtor should bear the costs of the Creditors Committee is in practical terms very difficult to implement, and is in any case a questionable goal.

