

## **RESEARCH PAPER**

# **LATIN AMERICAN INSOLVENCY SYSTEMS: ACTUAL DEVELOPMENTS AND CHALLENGES FACING THE NEW ECONOMIC AND TRADE REALITIES**

**AUTHOR:**

**RAÚL ALBERTO SUÁREZ ARCILA \***

[rausuar@yahoo.com](mailto:rausuar@yahoo.com)

**SUPERVISOR:**

**PROF. BOB WESSELS**

**LL.M. INTERNATIONAL BUSINESS LAW**

**VRIJE UNIVERSITEIT - AMSTERDAM**

**AMSTERDAM, THE NETHERLANDS, JUNE 2005**

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\* Raúl Alberto Suárez Arcila is a Colombian national, he obtained his Bachelor degree as a Lawyer (2003) at the “Universidad de San Buenaventura” in the city of Santiago de Cali, Republic of Colombia. He also obtained his LL.M. in International Business Law at the Vrije Universiteit – Amsterdam, The Netherlands with Honorific Mention (2005). The present paper was presented as a requirement to obtain the aforementioned LL.M degree.

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## PREFACE

The idea for this subject surged from my classes of International Insolvency Law, conducted by Professor Bob Wessels, in the context of the LL.M. in International Business Law at the Vrije Universiteit – Amsterdam, The Netherlands, in the spring of 2005.

I came from Colombia, which has been a country affected by many issues: the economic crisis my country has passed this many years, starting in the 80's with the crisis of the debt and the crisis of the financial sector, passing by the failing in the opening of the economy in the early 90's and the new crisis of the late 90's (political and economical), which I don't need to describe. I also was (and in fact still am) affected by the every day issues in all Latin America about the negotiations to create the Free Trade Area of the Americas, the end of the unilateral preferences to trade by the developed economies and the actually taking place negotiations between Latin American countries and the USA aimed to create Free Trade Agreements.

Also, the liberalization of the economies is something quite new for the most of the Latin American countries, new winds of integration are blowing, looking to overcome the big conglomerates conformed by multinational companies and companies with a strong position looking to open new markets, coming from developed economies and to confront trade negotiations in a way where those countries can make feel their presence.

All this, combined with my personal preference towards legal issues with regard to insolvency and the fact that many countries in the region are facing tough times, encouraged me select this topic too. To put it in another way: I wish to contribute with this research paper to gain a better insight and to promote the idea that the different countries should consider sincerely to adopt a more modern and efficient insolvency regime.

I do not pretend here to give a definitive opinion or to impose points of view, because as I have noticed while I was staying and studying here in Europe, people from different countries think different, even between people from individual countries from Latin America, every country has to think and to adopt solutions according to their own idiosyncrasy; also, I am not an specialist in the law of each and every country, so it would be daring to much to make definitive critics of the different systems. But, one thing I can provide is a more broader and systematic view. Quite regularly lawyers are seen as legal professionals with a narrow mind, focusing only on what the law and the judicial decisions of their own countries say. They often, in my opinion, lack a more critical approach, which is necessary for developing countries to go forward. With this study it is my modest aim to contribute to a better understanding of this necessity.

I hope you enjoy this paper and give me a feedback about it, which I am willing to improve taking into consideration your comments.

Finally, I would like to thank my supervisor Prof. Bob Wessels, for the support given to me, and also thank to Mr. Adolfo Rouillon, Senior Officer of the World Bank, for the support and materials which he provided me.

## INTRODUCTION

In the present Research Paper I will deal with the question: what are the challenges facing the Latin American countries in terms of their Insolvency systems in the new economic and trade reality?

For this purpose, I will divide this paper into different chapters and sections:

In the first chapter I will focus on mentioning and explaining the new economic and trade realities facing the Latin American countries, like the liberalization of their economies, the free trade agreements, and the regional and worldwide organizations; this chapter will not be related to legal issues of insolvency, but only to economic issues, which often form the context of any insolvency though. Also to describe how the new economic and trade realities have affected the Latin American countries to a point that many of them have started to change their legislative framework to adopt it to an environment of open economy and by that way to achieve the goals of healthy economies with improvement of living standards for the population.

In the second chapter I will give some general introductory remarks about the history of the development of insolvency systems in Latin America.

In the third chapter, I will focus on giving some details about the different legislations actually in force related to insolvency in different Latin American countries, the main body of the paper will contain some general characteristics of every system, and as a question of method, I will give more details of each system at the end of the paper, as annexes. In order to do this, I will choose the main countries, according to their GDP, of documents released by the International Monetary Fund, and international treaties dealing with insolvency regimes.

In the fourth chapter, I will give a brief theoretical approach towards modern insolvency regimes, and next, I will, based on the results in the previous chapters, point out the challenges, possible reforms and positive points to be accomplished in the different Latin American countries, with relation to civil law and insolvency law. In providing my view I will not only use a comparative view among them, but also point out international initiatives.

To finalize, I will conclude the present paper by giving an answer to the research question concerning the challenges of the insolvency systems in the Latin American countries, in terms of the new economic and trade reality.

I must clarify that the paper will be focused only to general insolvency regimes, and will not deal with special insolvency regimes such as the used for banks, or insurance companies, or financial institutions in general, and State owned enterprises. I must clarify also, that I will use the term insolvency proceeding (s) in this paper to refer to both liquidation and reorganization proceedings, and when I need to be specific, I will refer to the regime explicitly by referring either to a bankruptcy or liquidation proceeding or to a reorganization or rehabilitation proceeding.

## CHAPTER I:

### NEW ECONOMIC AND TRADE REALITIES

The liberalization of trade<sup>1</sup> and the new economic realities of the world have led to the Latin American countries to be in the “eye of the storm”, because they are considered as emerging economies in way to integrate to the world economy. The new economic and trade realities, as I call the actual situation with the emergence of democracy, liberalization of economies, and the effect in economies of the multilateral institutions like the World Trade Organization (WTO), International Monetary Fund (IMF) and others, and its consequences have not come free for those countries<sup>2</sup>, which have been passing since the 1980’s from financial crisis to political and social crisis with huge changes, and also have affected its growth and face them with external debt overhang, lack of access to investments, and losing the acquisitive power capacity of its residents. But, in the end, for Latin American countries many of the experiences of liberalization have become a symbol of economic progress, after years to change the rule of their markets.

The main factors that hinder trade related to Latin American countries are the uncontrolled public spending, the high inflation rates, excessive public debt, and the volatility of the exchange rates. In simple terms, the latter makes the exports and imports less or more attractive, in its domestic markets (in the case of imports), and in the foreign markets (in the case of its exports), producing instability in the trade balance and in the balance of payments, and making the external debt even more expensive to pay; all of this interfering with sound and stable long term economic policies and interfering with the trust of local and external financial sources to provide finance for new economic and trade expansion. The solutions for those problems are not likely to be applied by governments, which are, in most cases, restrictive trade or exchange policies.

Another factor that aggravated the situation in Latin America, has been the lack of supervision of some sectors of the economy, specially the banking sector, which was receiver of soft and accommodated policies and high levels of corruption (not to say that most banks were property of the State), and which, once in crisis, took over the productive sectors of the economy, mostly by restricting finance. The situation today, in

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<sup>1</sup> Based on: “The trade, debt and finance nexus: at the cross-road of micro- and macroeconomics”. Discussion Paper No. 06. Marc Auboin. World Trade Organization. 2004. [http://www.wto.org/english/res\\_e/booksp\\_e/discussion\\_papers6\\_e.pdf](http://www.wto.org/english/res_e/booksp_e/discussion_papers6_e.pdf) (Visited on 2 May 2005).

<sup>2</sup> For more specific information about this issue, please check: “Estudio Económico de América Latina y el Caribe – 2003 - 2004”, Capítulo V. ECLAC (CEPAL). 2004. [http://www.eclac.cl/publicaciones/DesarrolloEconomico/5/LCG2255PE/lcg2255\\_e\\_V.pdf](http://www.eclac.cl/publicaciones/DesarrolloEconomico/5/LCG2255PE/lcg2255_e_V.pdf) (Visited on 2 May 2005).

most or all cases, is under control. To make the situation even worse, world economic problems in the 1990's (case of the Asian countries, for example), especially with the Latin American trading partners, didn't contribute to a sound recovery.

Now, before continuing, I consider important to mention why trade liberalization is considered healthy for economies:

- 1) It strengthens external viability by improving exports competitiveness: by reducing export controls and requirements for domestic producers, measures which in time, decrease costs of production and make domestic products cheaper and competitive in international trade.
- 2) It improves efficiency of resource allocation and stability of external accounts: by eliminating distortions created by protectionist measures which can give more opportunities to one sector over others. Therefore, trade liberalization promotes the potential of explosion of real economic growth.
- 3) It helps to improve transparency and governance: by eliminating administrative costs and complex procedures.

In specific terms, this trade liberalization, and the efforts to integrate the Latin American countries to world economy have meant the adoption of some policies<sup>3</sup> like the introduction of independent supervisory bodies to specific sectors of the economy, with emphasis in the financial sector. Furthermore, trade liberalization has led to the introduction of policies to promote savings and investments, policies to promote access of natural and institutional investors to a more efficient and secure financial market, to the reforms in tax and tariff structures with the reduction of exemptions and privileged regimes, to the adoption of policies to control inflation rates. In addition it has made stronger the role of independent central banks, gradually eliminated subsidies and reduced the size of the public sector and reformed the laws related to budget and public expenditure. Other advantages include the increase in the amount of external reserves, and policies to promote employment, reforms on laws related to insolvency systems, and finally, but not lastly, membership to international institutions.

The results of liberalization for many domestic companies have been different: the arrival of external competitors, the mispreparation and the strengthening in policies, have led the companies to adopt for drastic solutions: to continue functioning in a highly competitive environment, to apply for reorganization or as a last solution, to bankruptcy proceedings, or to merge or be acquired in order to be sufficiently structured as to compete with big and/or prepared economic conglomerates.

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<sup>3</sup> For more information about a general framework of economic policies introduced, and to be introduced in Latin American countries, please check: "Opening Session of the ECLAC-IMF Round Table Seminar on Building Prosperity in Latin America and the Caribbean: Macroeconomic and Reform Priorities". Remarks by Mr. Rodrigo de Rato, Managing Director – IMF. May 30, 2005. <http://www.imf.org/external/np/speeches/2005/053005.htm> (Visited on 8 June 2005).

Moreover, the private and public sectors of the different Latin American countries agreed in one thing in particular: strengthening the integration with their commercial partners. As a result, a number of regional and bilateral agreements<sup>4</sup> have been signed and strengthened; Free Trade Agreements (FTA's) have been signed with the European Union, the United States of America, some Asian countries, neighboring countries, and regional initiatives (Regional Trade Agreements – RTA's) have acquired new pulse, like the Andean Community and Mercosur, and the actual negotiation of the Free Trade Area of the Americas (FTAA – ALCA).

For the purposes of trade agreements in which a country participates<sup>5</sup>, it is not important the number, but the proportion of world trade that such agreements can cover, also, the new trade reality comes from the late 1980's and 1990's, with the uncertainty provoked by the Uruguay round and therefore of a possible failure of multilateral trade negotiations and establishment of a forum for those. In the case of developing countries, including Latin American, the increase in trade agreements is also a result of the decrease in preferential regimes adopted unilaterally by developed economies (or WTO members in general) or the gradual decisions of the WTO to eliminate those, under the argument that are forms of subsidy and discrimination contrary to the objectives of the GATT and GATS. As a result, trade agreements have become more complex, with provisions going beyond mere trade, following provisions for strategic market access, and, if the agreement consists in forming a customs union, to establish a common external tariff and harmonization of external trade policies.

The efforts in trade agreements in Latin America have been successful if one considers the steps taken to integrate the MERCOSUR and Andean Community, steps that in the medium term will end with the merger of the two blocs, creating the South American Community of Nations<sup>6</sup>, the agreement to create an FTA between Andean and Mercosur countries, the fact that Mexico applied for an associate membership on Mercosur as well as signed an FTA with Japan, and it's part of the NAFTA. The USA has signed an FTA with the Central American countries, approved an FTA with Chile, and is in negotiations with Andean countries (Colombia, Peru, and Ecuador). Mercosur has signed an FTA with India, Panama is negotiating with Singapore, and Chile has signed an FTA with the Republic of Korea, etc. Finally, the most comprehensive in the region is the negotiation of the Free Trade Area of the Americas (FTAA – ALCA)<sup>7</sup>.

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<sup>4</sup> Based on: "The Changing Landscape of Regional Trade Agreements". Discussion Paper No. 08. Jo-Ann Crawford & Roberto V. Fiorentino. World Trade Organization. 2005. [http://www.wto.org/english/res\\_e/booksp\\_e/discussion\\_papers8\\_e.pdf](http://www.wto.org/english/res_e/booksp_e/discussion_papers8_e.pdf) (Visited on 2 May 2005).

<sup>5</sup> Based on: "Informe sobre el Estado de la Integración 2003 – Situación de los Procesos de Integración en América Latina: Avances y Desafíos". Convenio Andrés Bello – Instituto Internacional de Integración. 2004. <http://www.iiicab.org.bo/libros/uno2.pdf> (Visited on 2 May 2005).

<sup>6</sup> See: <http://www.comunidadandina.org/ingles/press/np3-12-04.htm> (Visited on 7 June 2005).

<sup>7</sup> See: <http://www.ftaa-alca.org> (Visited on 7 June 2005).

The efforts by now, in Latin America, are centered in achieving a sub regional positive integration to face the FTAA<sup>8</sup>, which could bring, if it's not well negotiated, not an opportunity to achieve many positive social and economic goals, but a regional disequilibrium between the North (USA and Canada) and the South (Central and South America), perpetuating the historic dependency of the latter bloc with the former, especially by leading the Latin American countries to a position where many of them were in the early 90's, when, trying to liberalize their economies, didn't take into consideration several aspects which lead to the collapse of its financial and productive infrastructure, leading them to economic crisis that have taken years to overcome.

The "Sutherland Report"<sup>9</sup>, sponsored by the WTO has recognized the new economic and trade realities, and has proposed several recommendations to the WTO as organization and to its Member States, like the awareness to governments to avoid harming the non discriminatory, most favoured nation (MFN) treatment, base of the multilateral trading system, and by that way to avoid benefits of trading partners by harming those outside. Another recommendation is to subject preferential trade agreements to more controls using the Trade Policy Review Mechanism to avoid excessive benefits through them. Another recommendation is the call to other international institutions to act jointly with the WTO to design strategies to improve trade policies in developing countries, etc.

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<sup>8</sup> Based on: "El Área de Libre Comercio de las Américas (ALCA) y sus Repercusiones en América Latina". Instituto Internacional de Integración. 2003. <http://www.iiicab.org.bo/libros/Libro2.pdf> (Visited on 2 May 2005).

<sup>9</sup> "The Future of the WTO: Addressing Institutional Challenges in the New Millennium". (Also known as Sutherland Report). World Trade Organization (WTO). 2004. [http://www.wto.org/english/thewto\\_e/10anniv\\_e/future\\_wto\\_e.pdf](http://www.wto.org/english/thewto_e/10anniv_e/future_wto_e.pdf) (Visited on 2 May 2005).

**CHAPTER II:**

**HISTORICAL BACKGROUND OF THE INSOLVENCY SYSTEMS IN  
LATIN AMERICA**

The contribution of the American continent to the internationalization of domestic laws is indisputable. In this context I can mention two important contributors: the Inter American Conferences, and, since 1948, the Organization of American States (OAS).

The efforts to unify legislation and to achieve a system of laws in the American countries, dates from early 1824, when Simon Bolivar convoked the so called “Congress of Panama” (or Congreso de Panama), and which was held between 22 June and 15 July 1826. The practical effect of this Congress, for the purposes of this paper, was the introduction of a motion to start soon with the codification of provisions of private international law.

Starting from this point, the American practice to codify international law, has been continuous. The effort to create the codification can be divided into two stages: idealism and pragmatism. In the stage of idealism, which preceded the European movements for unification of laws, and on it, the American States started an ambitious project of global codification of private international law, the first result of which was a treaty signed in Lima, Peru in 1878, which, it’s worth to mention, didn’t entered into effect.

As a response to this failure, ten years later, in 1888, the Minister of Foreign Affairs of the Republic of Argentina and the Envoy Extraordinary and Minister Plenipotentiary of the Oriental Republic of Uruguay, met in Buenos Aires (Argentina), to consider calling a meeting of all the legal advisers of all the governments of South America. As a result the so called “Congress of Montevideo” (Congreso de Montevideo) was convened, to which were invited the governments of Chile, Brazil, Peru, Bolivia, Ecuador, Colombia Venezuela and Paraguay; the Congress lasted until 18 February 1889, and the results were different independent treaties, regulating different subjects, among them, insolvency<sup>10</sup> (or bankruptcy to refer to the exact term used in the treaties). Those treaties were revised in 1940, 1979 and 1989, but the only treaties referring to insolvency were the ones of 1889 and 1940.

The Montevideo Treaty of 1889, marked the efforts to try to unify legislations after the independence of Latin American States, which had started by taking different ways, when before they had similar provisions. The similarity of law reflected the legacy of Spain and Portugal, which in turn were part of the Roman legal family. This treaty followed the system of the domicile of the company. The opening of what we now call secondary or ancillary proceedings was almost inexistent, because, most of the proceedings were opened as main or principal proceedings. Also certain amount of court to court

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<sup>10</sup> Ratified by: Argentina, Bolivia, Paraguay, Peru, and Uruguay. Adhered later by Colombia.

communication was achieved, and the authority of the Liquidators also had to be recognized in all the States.

The Montevideo Treaty of 1940 introduced some interesting issues<sup>11</sup>, but mostly what it did was to change some words, to clarify some of the terms and to integrate whole articles or parts of an article into another. Furthermore the Treaty added an explicit definition of the commercial domicile (Art. 3), changed the name from “falency” to “bankruptcy” (Title VIII), and introduced the publication of the declaration of bankruptcy and other acts concerning the bankruptcy in the States where the debtor has agencies, branches or establishments (Art. 42). Moreover the Treaty provided for recognition in local procedures of the existence of different institutions or procedures related to bankruptcy (Art. 45), made explicit reference to the “preventive concordat”, and added an element that for me is a violation to the principle of “par conditio creditorum”, meaning that *“debts located in a State have preference with respect to the debts located in another, over the mass of assets corresponding to the State of its location”* (Art. 48).

In my point of view, this last treaty only clarified some points that could easily be clarified by the authorities of the different States parties of the treaty of 1889, and, maybe that is why it was only ratified by few countries, having a similar legal tradition, because all of them were part of the former Republic of Rio de la Plata.

From this point forward, the Pan American Conferences had an important role; they constituted an important forum to discuss economic and political issues. Law was a secondary issue. But taking into consideration their effort to achieve unions, economical and political, in 1928, in the framework of the 6<sup>th</sup> Pan American Conference in La Havana, Cuba, a code of private international law was approved. This code was named “Bustamante Code”<sup>12</sup> (or Código Bustamante), and was named like, after a motion of the Nicaraguan delegation in honor of the prominent Cuban legal scholar: Dr. Antonio Sanchez de Bustamante y Sirvén. Its importance was that it was the first complete code referring to the conflicts of laws in different subjects, and a relevant effort in the unification of laws. This code was marked by the predominance of the universality of insolvency proceedings, except where there were economic independent establishments of the debtor located in another country, rights in rem on debtor’s assets located in another country, or only one commercial domicile of the debtor; and also marked by the ample field of action to the public policy and the division of laws between public and private.

Finally, it was too much to ask for this Code, their provisions were very advanced for its time, as it can be seen from the Reservation made by Colombia and Costa Rica<sup>13</sup> when signing the treaty, mainly because those countries pointed that they didn’t want a new

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<sup>11</sup> Ratified by Argentina, Paraguay and Uruguay.

<sup>12</sup> Ratified by: Bolivia, Brazil, Chile, Costa Rica, Cuba, Dominican Republic, Ecuador, El Salvador, Guatemala, Haiti, Honduras, Nicaragua, Panama, Peru, and Venezuela.

<sup>13</sup> See: <http://www.oas.org/juridico/english/sigs/a-31.html>

European colonialism and, they wanted also to preserve the doctrine of domicile, main characteristic of the Latin American legal systems by the time.

In the second stage, pragmatism, since the early 1970's in the framework of the OAS (Inter American Conferences on Private International Law and the Inter American Council of Jurists), the global codification marked by the Bustamante Code had been left behind to focus on efforts in the treatment of different issues separately. This policy was chosen, due to the facilitation in the national context to deal and ratify separated issues, rather than full codifications with complex and long declarations and reservations.

In the national sphere, the different Latin American countries have had provisions in the past mostly in their civil and commercial codes, marked by the predominance of the doctrine of domicile, the separation between natural and legal persons, and traders or non traders in terms of insolvency regimes. The effects of the aforementioned treaties in the national legislations of Latin American countries were very deep, as to the point that those legislations have been changed and the provisions of those treaties, in one or another way were introduced into them. Today's insolvency regimes, still keep some elements of the past, but as we will see in this paper, they are changing to adapt to the new economic and trade realities.

## CHAPTER III:

### ACTUAL LEGISLATION RELATED TO INSOLVENCY IN LATIN AMERICA

The actual developments of legislation in different countries of Latin America, are taking a similar path: the introduction of separate legislation is taking force among those countries, due to the incapacity of the Codes (also in terms of physical space) to contain such specific and detailed legislation. Also in terms of cross border insolvency, although the most predictable future is the adoption of a pragmatic approach (with the adoption of the UNCITRAL Model Law on Cross Border Insolvency).

However, they present certain important differences and have some important characteristics that for the purposes of this paper are important to be outlined. In the next sections of this chapter I will provide those differences and characteristics, focusing on countries which for the size of its economy or its perspectives (growing potential and strategic geographic location, as well as source of raw materials, etc)<sup>14</sup> have an important playing role, not only in Latin America, but worldwide; those countries are: for South America, Argentina, Brazil, Chile, Colombia, and Venezuela, and for Central America, Costa Rica and Mexico.

#### SECTION 1. ARGENTINA:

##### 1.1. GENERAL REMARKS:

The Argentinean law<sup>15</sup> dealing with insolvency dates from 1995 and is the law No. 24.522.

The Argentinean position in terms of insolvency is very important nowadays, taking into account the political and economical crisis suffered by the country in the late 20<sup>th</sup> century and early 21<sup>st</sup> century, which exploded because of several causes like the parity of the exchange rate of 1:1 relation between the Argentinean Peso and the US Dollar for almost eleven years, the emergency in the banking system, and the inability of the Argentinean

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<sup>14</sup> Sources:

- "Estudio economico de America Latina y el Caribe 2003 – 2004". [http://www.eclac.cl/publicaciones/DesarrolloEconomico/5/LCG2255PE/lcg2255\\_e\\_V.pdf](http://www.eclac.cl/publicaciones/DesarrolloEconomico/5/LCG2255PE/lcg2255_e_V.pdf) (Visited on 2 May 2005).
- "Indicadores de la Comunidad Andina, Mercosur y Chile 1994 – 2003". <http://www.comunidadandina.org/estadisticas/SGde085.pdf> (Visited on 2 May 2005).
- Table 6(concluded). "World Economic Outlook: Statistical Appendix -- April 2005". Pag. 211. <http://www.imf.org/external/pubs/ft/weo/2005/01/pdf/statappx.pdf> (Visited on 2 May 2005).

<sup>15</sup> Amended by other several laws like Nos. 24.760, 25.113, 25.563, and finishing with the law No. 25.589 of May 16, 2002.

government to reduce the fiscal deficit, etc. The crisis in a major or minor measure continues today.

The aforementioned recession took to the limit the conventional dispute resolution methods, like the individual methods stated in the different Civil and Commercial Codes, and collective methods stated in specialized laws like the one of insolvency No. 24.522 of the year 1995. For this reason, special laws to deal with the crisis were enacted, like the law 25.563 enacted on 14 February 2002 and valid until 10 December 2003, which established emergency procedures to help with the stabilization of the corporate sector<sup>16</sup>, among which it can be found:

- a) The period for the debtor to submit a composition plan to its creditors, and avoid bankruptcy declaration was extended from its originally 30 days to 180 days, extendable for a second equal term.
- b) Suspension of foreclosures and pledges against debtors, within reorganization procedures, for a term of 180 days.
- c) Suspension for a term of 180 days, of bankruptcy petitions against a debtor, except to request precautionary measures.
- d) An extension of one (1) year for all debtors to fulfill their obligations under composition procedures.
- e) A composition plan of a debtor could encompass payment of less than 40% of the general claims existing in the moment of the filling of the procedure.
- f) To the financial institutions, a term of ninety (90) days to reschedule their credits with debtors were given; this new reschedule had to be given by a new agreement taking into consideration the new financial regulations (specially the called “corralito financiero” or limit to withdrawals).
- g) All forced execution proceedings, save some cases, were suspended for a term of 180 days.
- h) All acts of disposal of assets beyond the ordinary course of businesses and during the period of suspension would be null and void unless expressly authorized by creditors.

After this law, the law No. 25.589 of 16 May 2002 was enacted normalizing the situation. Next I will describe<sup>17</sup> some important characteristics of the Argentinean Bankruptcy law No. 24.522 as amended by the law 25.589:

- The suspension of payments (defined as impossibility to pay debts) is a requirement to initiate insolvency proceedings, and those insolvency proceedings apply to all the assets of the debtor.

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<sup>16</sup> “Argentine financial emergency legal framework”. Brons & Salas Abogados. 2002. <http://www.iiiglobal.org/country/argentina/emergency.pdf> (Visited on 2 May 2005).

<sup>17</sup> “Report on the Observance of Standards and Codes – Argentina. Insolvency and Creditor Rights systems”. World Bank, June 2002. [http://www.worldbank.org/ifa/icr\\_arg.pdf](http://www.worldbank.org/ifa/icr_arg.pdf) (Visited on 2 May 2005).

- The parties subject to insolvency proceedings are natural persons (different than in other countries of Latin America, which handle this issue as a matter of private law according to their Civil Code), and legal persons, even legal persons where the government has a participation, no matter the percentage, except some express exception ruled by law. Some special cases are also the estate of a deceased person, and debtors domiciled abroad with respect of assets in the country.

- The system to determine the competent Court is depending of a) the main administrative offices (HQ's), the domicile, or the main place of business. Failing to ascertain such requirements, the Court that first heard the case should be taken as competent.

- The different proceedings stated in the bankruptcy law are: liquidation (quiebra) and reorganization (concurso preventivo). A liquidation process can be voluntary (when initiated by a debtor) and involuntary or necessary (when initiated by a creditor or after a frustrated reorganization procedure).

- The effects of the declaration of one of those proceedings are: first, automatic suspension of any undecided or pending actions filed by creditors related to rights and interests in the bankrupt estate, second, a stay on the calculation of interest is imposed.

- The insolvency proceedings are concluded in several ways: first, when there are no more assets to distribute to creditors, in such case the liquidator (síndico) has to file a petition to the court to conclude proceedings (clausura por falta de activos). Second, when the debtor has obtained the unanimous consent of all creditors (avenimiento). Third, after the selling of all assets, which can take from several months to several years.

- The rank of credits under the bankruptcy law is: first, specially privileged credits ("créditos con privilegio especial"); second, administrative expenses ("gastos de conservación y de justicia"); third, ordinary privileged credits regarding to labor ("créditos con privilegio general laboral"); fourth, ordinarily privileged credits not related to labor ("créditos con privilegio general, no laboral"); fifth, the ordinary, common and unsecured credits ("créditos quirografarios o communes"); sixth, the conventionally subordinated credits ("créditos subordinados"); seventh, foreign credits payable after all others have been settled ("créditos extranjeros subordinados al saldo"); eighth, the holders of equity ("socios") of the bankrupt company.

- The Judge is the "director" of the process, therefore, he is entitled to investigate and deal with fraud, illegal activities and abuse of the bankruptcy system.

For more details about the insolvency system in Argentina, please check the Annex I of this paper.

## **1.2. INTERNATIONAL INSOLVENCY ISSUES:**

The international insolvency issues are treated within Argentinean law taking into consideration the Montevideo Treaties of 1889 and 1940 (which bind Argentina only with the countries that have ratified those Treaties), and other provisions of conflict of laws contained in domestic legislation (arts. 2, 3, 4 Bankruptcy law).

The rule of local preference, which subordinates the credits from foreign bankruptcy proceedings, is only applicable in insolvency proceedings.

The ranking of all priorities should be governed by “lex fori” (Argentine law), when proceedings have been initiated in Argentina. The effect of such proceeding is territorial, and therefore, limited to the Argentinean territory.

## **SECTION 2. BRAZIL:**

### **2.1. GENERAL REMARKS:**

The South American giant, from the economic point of view had been facing problems of unemployment and low growth, also in 1999 faced a currency crisis; despite all this, the country has been recovering, but still has to fight against external problems like adverse conditions due to a weak global environment and the risk associated with emerging markets. After 2003, the change to a left wing democracy has been, it seems, having good effects in the economy, due to some positive developments; with them, the confidence has come back, the path to sustained development has been clarified, the inflation has been kept under control, and consumption and production have rebounded<sup>18</sup>. In the last four years, the effort has been focused also in the strengthening of policies and institutions.

The new bankruptcy law<sup>19</sup> (of February 2005) aims to preserve the assets of bankrupt firms in a business oriented way, assuring creditor’s rights and creating a field for the viable companies to reassume activities, while creating a good environment for the attraction of investments.

The former insolvency regime was governed by the Federal Decree Law No. 7.661 of 1945, next I am going to give a brief description of this regime; my aim is to make visible the differences between the former and the new regime. Under this regime<sup>20</sup>, only certain persons defined as merchants (legal or natural persons), specially corporations and limited

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<sup>18</sup> “Trade Policy Review – Brazil”. World Trade Organization, Document No. WT/TPR/G/1401. November 2004.

<sup>19</sup> Source: - Lei No. 11.101 de 9 de Fevereiro de 2005 “Regula a recuperação judicial, a extrajudicial e a falência do empresário e da sociedade empresária”. <http://www6.senado.gov.br/legislacao/ListaPublicacoes.action?id=250164> (Visited on 2 May 2005).

<sup>20</sup> “Insolvency and restructuring in Brazil”. By Felsberg e Associados. <http://www.iiiglobal.org/country/brazil/insovrestructbrazil.pdf> (Visited on 2 May 2005).

liability partnerships were covered, other persons, not defined as such, are considered as civil persons, and provisions of the Civil Code are applicable. Also excepted from this regime were companies like public and private joint stock corporations with participation of the government (*sociedades de economia mista*), financial institutions and insurance companies.

Also, the proceedings were different: insolvency, bankruptcy and concordata (which could also be preventive and suspensive).

The parties authorized to file for insolvency proceedings were the creditors, the debtor (under a voluntary insolvency procedure), and a partner or shareholder; and in case of natural persons, the surviving spouse, the heirs, and the administrator of the estate.

The administration of the insolvency proceeding under this regime, was competence of the State Court where the debtor had his registered headquarters, exercising jurisdiction in cases where the directors of the company resided outside its regional jurisdiction by a Commission (*precatória*), or if they reside abroad by a rogatory letter (*carta rogatória*). The Court also had the power to appoint a liquidator (*síndico*), in the case of bankruptcy proceedings, or an inspector (*comissário*), in the case of a concordata (reorganization proceeding).

Next I will describe some characteristics of the actual bankruptcy legislation, Law No. 11.101 of February 9, 2005:

- The law applies for bankruptcy procedures, judicial and extra judicial reorganization procedures.

- The law doesn't apply to public companies (*empresas públicas*) or companies with participation of the State (*empresas de economia mista*), financial institutions, insurance companies, cooperatives, or similar.

- The competent Court for the proceedings referred in this law is the one with jurisdiction where the main establishment of the debtor is located, or where the branch of a company incorporated outside of Brazil is located.

- The decree of insolvency or the granting of the processing of the judicial recovery suspends the term of prescription of all the judicial proceedings and executions against the debtor (for a unique term of 180 days, after which the actions suspended can proceed or be initiated new actions by the creditors). The processes which are dealing with illiquid amounts will continue, and actions related to the employment contract are to be dealt by the specialized justice.

- In general terms, the obligations with the tax authorities are not suspended with the decree of insolvency or the granting of the processing of the judicial recovery.

- In the proceedings referred in the bankruptcy law, the main organs appearing in such procedures are: the Court, the Judicial Administrator, the Creditors' Committee, and the Creditors' General Assembly.

- The verification of the credits of the debtor and the consolidation of the final table of credits and creditors are functions of the judicial administrator, which is a certified professional, natural or legal person (in this case, will be selected a natural person to be responsible for the process), and the Court in this case has a function of homologation of those. The judicial administrator also has other more specific functions, which I will describe in the next sections.

- The creditors' committee is conformed by representatives of: the employees of the debtor (credores trabalhistas), of creditors with rights in rem, guarantees or special privileges, and of common and unsecured creditors. If there is not creditors' committee, the judicial administrator or, the judge, will exercise its functions.

For more details about the insolvency system in Brazil, please check the Annex II of this paper.

## **2.2. INTERNATIONAL INSOLVENCY ISSUES:**

Despite this law is very new and there is no judicial decisions according to its spirit, it can be mentioned that the Bustamante Code is still applicable between the parts that have ratified it, including Brazil; also that according to this law, the assets located in Brazil are governed by Brazilian law; this means that to deal with them, the procedure to open is the one referred in the new bankruptcy law.

For the moment, the UNCITRAL model law<sup>21</sup> or similar provisions have not been adopted de deal with transnational insolvencies<sup>22</sup>.

## **SECTION 3. CHILE:**

### **3.1. GENERAL REMARKS:**

Chile is a special case in Latin America<sup>23</sup>. Surrounded by economical and political instability of its neighbor countries, Chile has managed to survive and to convert itself in

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<sup>21</sup> See: <http://www.uncitral.org/en-index.htm> (Visited on 20 May 2005).

<sup>22</sup> "Cross Border Insolvencies and Restructuring in Brazil". Thomas Benes Felsberg. [http://www.iiiglobal.org/country/brazil/Cross%20Border%20\(012703\)%202.pdf](http://www.iiiglobal.org/country/brazil/Cross%20Border%20(012703)%202.pdf) (Visited on 2 May 2005).

<sup>23</sup> Based on: - Ley No. 18.175/82, modified by Ley 19.806/02. Biblioteca del Congreso Nacional (Chile).

if not the only one, at least one of the most stable countries of the region, both in political and economic terms.

In 1973 the Marxist government of Salvador Allende was overthrown by a coup d'etat led by the then General Augusto Pinochet, who installed a military government, which lasted until 1990. This regime was followed by a Socialist Democratic government led by Mr. Ricardo Lagos, which in conjunction has enacted sound economic policies and has guided the country to a liberalized market economy with sustained economic growth<sup>24</sup>.

However, in trade topics, the position of the country has been the one of an outsider of the region. In fact, Chile has been separated from the multilateral integration processes like Mercosur or the Andean Community, to conduct a different policy based mostly in bilateral treaties, exemplified by the latest with the United States of America and the European Union.

Now, referring to Chile's insolvency regime, the laws governing it are: Law No. 18.175 of 1982, and the Law No. 19.806 of 2002. Next I will describe some important characteristics of the regime:

- The Chilean insolvency regime is considered as independent and reliable, also, it is considered to be well integrated with the rest of commercial and legal system, and with a well balanced system of liquidation and reorganization. In addition, there isn't specialized insolvency Court, but those matters are dealt by general civil courts, and, an independent third party (the receiver) is appointed in each proceeding to represent interest of creditors or to manage the assets of the insolvent debtor. Despite all this, there are some negative points which make the Chilean legislation unpleasant, like provisions of cross border insolvency, recognition of foreign awards, inexistence of non judicial enforcement methods, and the slow advance of the judiciary to enforce or to solve different proceedings.
- The bankruptcy law is applicable to natural and legal persons, with the exception of banks, financial institutions, insurance companies, State owned enterprises and mixed companies (Empresas de economía mixta), where the State is the majority shareholder.
- The bankruptcy procedure can be requested by the debtor itself or by one or more of his creditors.
- The mortgagees and other secured creditors in general terms can, despite the initiation of bankruptcy proceedings, enforce their rights in separate proceedings to obtain the payment of their credits.

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[http://www.bcn.cl/publicadores/pub\\_leyes\\_mas\\_soli/admin/ver\\_archivo\\_ultimas.php?id\\_ultima=165](http://www.bcn.cl/publicadores/pub_leyes_mas_soli/admin/ver_archivo_ultimas.php?id_ultima=165) (Visited on 2 May 2005).

- The 2 proceedings covered by bankruptcy law are: reorganization (convenio judicial preventivo) and bankruptcy (quiebra). There is also a method, in which during the bankruptcy proceeding the debtor and unsecured creditors can negotiate a reorganization plan, which can be preventive (preventive) or simply judicial (convenio simplemente judicial) to end the bankruptcy proceeding.

- The Bankruptcy Superintendence (Superintendencia de Quiebras) is an independent and technical body in charge of supervising the receivers (Síndicos) in legal, financial and technical way. It also has an active role in the bankruptcy proceedings, like the petition to the Court to suspend or remove a receiver, and in statistical and technical matters, like taking the registry of bankruptcies, and advising the Ministry of Justice to present reforms to legislation related to its competence.

For more details about the insolvency system in Chile, please check the Annex III of this paper.

### **3.2. INTERNATIONAL INSOLVENCY ISSUES:**

Chilean bankruptcy law doesn't regulate cross border insolvency proceedings<sup>25</sup>. The only provision relating to this issue refers to the creditors residing abroad.

If the Chilean Courts were confronted today with an issue relating a cross border insolvency, they should first check if Chile is part of an international agreement dealing insolvency with the State to which the requesting Court is part (like with the Bustamante Code); if a Treaty is not applicable, then the Court should refer to the principle of reciprocity, and as a last option, refer to the rules of conflict of laws of its national legislation.

The UNCITRAL Model Law has not been adopted up to the moment.

## **SECTION 4. COLOMBIA:**

### **4.1. GENERAL REMARKS:**

Colombia has a privileged position in Latin America, apart from its geographical important position, linking Central and South America, with coasts in the two (2) oceans (Atlantic and Pacific), and bordering important countries like Venezuela, Brazil, Ecuador,

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<sup>24</sup> "Indicadores de la Comunidad Andina, Mercosur y Chile 1994 – 2003". <http://www.comunidadandina.org/estadisticas/SGde085.pdf> (Visited on 2 May 2005).

<sup>25</sup> "Chilean Legislation and Cross Border Insolvency". Ricardo Sandoval. From: Texas International Law Journal. Summer 1998. <http://international.westlaw.com/Find/Default.wl?rs=WLIN1.0&vr=2.0&FindType=0&SerialNum=0110540206> (Visited on 2 May 2005).

Perú and Panamá; and besides, a political paradise between the countries of South America due to the political stability of its leaders democratically elected. Despite all this, which gives the country a high probability of being a receiver of investment, the armed conflict with guerrillas, self defenses (paramilitaries) and drug dealers, has sabotaged its possibilities.

In addition, the country, with a recently liberalized economy (1990's) has faced several economic crises which have taken away investment opportunities, but which also, gave birth to effective insolvency legislations. In fact, the political plurality of the country has allowed the birth of insolvency legislation with a very good mix of economic and socially protective aims, and also very flexible, as is shown in the preparatory works of the law 550 of 1999. With this, I am not saying that the legislation is perfect, because as is true that it has been very effective, there are many aspects than can be improved; this postulate has been understood with the enacting of the law 922 of 2004, which extends the duration of the law 550 of 1999 and in its preparatory works, mentions that is only a measure to give more time to the government to finish preparing a more complete and precise law, which by the time the law 550 of 1999 was supposed to end, was still not finished.

Now, in Colombia, the legislation related to insolvency is covered by the law 222 of 1995, dealing with the mandatory insolvency proceeding and a judicial reorganization proceeding called concordat (concordato preventivo); after this law, and taking into consideration that the aforementioned law had difficulties to deal with the economic crisis of 1998, was enacted the law 550 of 1999, with a purely contractual reorganization proceeding called restructuration proceeding (acuerdo de reestructuración) and where the State intervenes very few times, and lastly, the law 922 of 2004 that extends the period of validity of the law 550 of 1999. Also, those laws are integrated with the Civil and Commercial Codes. The aforementioned laws regulate the insolvency and reorganization of the persons (natural and legal) that the legislation considers as traders, for the other persons that are not considered as traders, the insolvency and reorganization are dealt within the Civil Code.

Next I will mention some characteristics of the Colombian insolvency proceedings:

- All the patrimony of the debtor is subject to insolvency proceedings.
  
- All the reorganization proceedings are extrajudicial, because the restructuration agreement is considered as a contract between the debtor and his creditors, and the judiciary doesn't participate, the State is represented by the Superintendence of Companies. The exception to this is the preventive concordat and the liquidation of non traders, in which the Civil Circuit Court (Juez Civil de Circuito) is the competent to deal.

In exceptional cases, the competent to deal with reorganization proceedings (restructuration agreement) are the Chamber of Commerce of the domicile of the debtor,

other Superintendences and, in the case of public entities, the Public Finance Ministry (Ministerio de Hacienda y Crédito Público).

- All the creditors, in the insolvency proceedings, are equal. The only difference is their preferences or privileges, which are dealt by the law.

- There is an independent and technical institution, called the Superintendence of Companies (Superintendencia de Sociedades), which is in charge of promoting the restructuring proceedings, and its supervision. It also has a jurisdictional function, in the sense that when the concordat proceeding is opened, the Courts dealing with executions and public entities executing for public debts against the debtor have to send those proceedings to the Superintendence for it to continue its process. In the other hand, in the liquidation proceeding, the Superintendence orders the privileged embargo of all the assets of the debtor.

- In the liquidation proceedings, a third party has the function to represent the debtor and to pay all the debts of the debtor with the debtor's assets; this party is called the liquidator (liquidador). In the preventive concordat the third party with the functions to promote and serve as bridge between the parties of the concordat and the State is called the receiver (contralor). In the restructuring proceeding the third party is called the promoter (promotor).

- The main difference between the two (2) modes of reorganization is that, in the restructuring agreement (Law 550/99) the agreement is between the creditors and the debtor in a voluntary way, giving more space to the debtor to negotiate and to go out of the crisis. In the concordat (Law 222/95) the debtor has less space to get a reorganization formula; it can be formulated by him, but has to be approved by the Creditors' Committee. In the other hand, the concordat doesn't necessarily suspend the preventive measures taken in a legal process, but the restructuring agreement does. Also, in the Concordat, the State has a more active role, while in the restructuring agreement the active role is more of the parties than of the State.

For more details about the insolvency system in Colombia, please check the Annex IV of this paper.

#### **4.2. INTERNATIONAL INSOLVENCY ISSUES:**

Colombia<sup>26</sup> has not adopted yet the UNCITRAL Model Law on Cross Border Insolvency. However, in the project of law of insolvency, which is still in study in the Superintendence of Companies, is under study the inclusion of the aforementioned model law.

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<sup>26</sup> - "Insolvency overview – Colombia". Global Insolvency Law Database. World Bank. <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/LAWANDJUSTICE/GILD/GILD>

In the moment, the administrators or liquidators in foreign insolvency proceedings are not recognized in the Colombian environment. However, the figure of the *exequatur* is available to recognized foreign judicial decisions.

The foreign creditors and credits are recognized without any problem in the Colombian insolvency proceedings.

Colombia is part of the Treaty of Montevideo of 1889, so the procedures mentioned there are binding between the parties of the Treaty.

## **SECTION 5. VENEZUELA:**

### **5.1. GENERAL REMARKS:**

The position of Venezuela<sup>27</sup> in Latin America is very important, especially because its huge oil reserves, which gives the country a status to attract multinational investments. Despite the big revenues derived from the oil industry, the public deficit is something to worry about; also, the political environment has distorted the flow of investments and the policy of the country towards trade liberalization<sup>28</sup>, with the opposition mainly composed of private companies and the argument of privation of fundamental civil rights.

More specifically talking about the insolvency system, it is regulated mostly in the Commercial Code of 1955, the Civil Code of 1982, and the Code of Civil Procedure of 1987. The proceedings available under Venezuelan law are insolvency (or bankruptcy) proceeding, and a procedure similar to reorganization called benefit of moratorium relief (*estado de atraso*), the latter procedure can be initiated if the debtor needs time to pay his debts due to a lack of liquidity caused by an unforeseeable event. There are also special insolvency regimes for some sectors like for the financial sector and public enterprises, and for natural persons, and those who qualify as non traders; to which, either is applicable a special law, or is applicable the Civil Code (proceedings like assignment for the benefit of creditors, and the general meeting of creditors to approve a reorganization plan).

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[COUNTRIES/GILDCOLOMBIA/0..contentMDK:20114082%7EmenuPK:262551%7EpagePK:157658%7EpiPK:157731%7EtheSitePK:262545.00.html](#) (Visited on 15 May 2005).

<sup>27</sup> “Insolvency in Venezuela”. Fernando Peláez-Pier, Carlos Dominguez-Hernandez and Yulena Sánchez-Hoet. <http://www.hpcd.com/en/abogados/download/Gettinthealthroughnov2005.pdf> (Visited on 2 May 2005).

<sup>28</sup> “Trade Policy Review – Venezuela”. Report by the Secretariat. WTO. 2002. [http://docsonline.wto.org/GEN\\_viewerwindow.asp?D:/DDFDOCUMENTS/T/WT/TPR/S108-0.DOC.HTM&skip=0](http://docsonline.wto.org/GEN_viewerwindow.asp?D:/DDFDOCUMENTS/T/WT/TPR/S108-0.DOC.HTM&skip=0) (Visited on 24 May 2005).

Indeed, the legislation which is of interest here is the applicable to companies, and not to individuals or special regimes, its worth to say that this legislation, as I mentioned can be found in the Commercial Code, which in the same time, articulates those provisions with the rest of the Code which is very old and is not very well prepared to deal with the problems arising today.

Next I will mention some characteristics<sup>29</sup> of the Venezuelan insolvency proceedings:

- The procedure can be started by the debtor or by any of his creditors, secured or not.
  
- Once the initiation of proceedings has been requested, the Court can order a freezing of all the assets (embargo), the suspension of all legal proceedings and executions against the debtor (for a maximum term of one (1) year; and which benefits all creditors, except tax creditors, secured or privileged creditors. The Court also has to appoint a receiver (Síndico). In addition, when bankruptcy is declared by the Court, all un-matured debts of the debtor are triggered and become payable.
  
- The competent Court to deal with the proceedings referred here is the Commercial Court, now assumed by the civil ordinary Courts (Jueces de primera instancia civil, mercantile y de tránsito) of the domicile of the debtor. Exceptionally, when the liabilities of the debtor are less than certain amount defined in the Codes, the competent Court would be the Municipal Court of the domicile of the debtor.
  
- For the liquidation proceeding, a suspension of payments is required, and also that the liabilities of the debtor exceed his assets.
  
- Under the benefit of moratorium relief, the debtor doesn't loose control of his assets, or its management, but his actions have to be reviewed by a third party appointed by the Court and by a surveillance committee composed by creditors. This is not the same when a bankruptcy proceeding has been opened, in which the debtor loses control over his assets, and also its management, can't dispose of them or assume any new obligations, all the decisions have to be taken by the receiver, who from that moment on represents the mass in liquidation.
  
- The moratorium relief period can not exceed of one (1) year, and can only be extended if the creditors with unpaid debts have arranged to do so.

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<sup>29</sup> Based on: - "Venezuela: insolvency under Venezuelan law". Carlos Acedo Sucre and Luisa Acedo De Lepervanche. 11 April 2005. <http://www.mondaq.com/article.asp?articleid=31915&lastestnews=1> (Visited on 2 May 2005).  
- "Insolvency overview – Venezuela". Global Insolvency Law Database. World Bank. [http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/LAWANDJUSTICE/GILD/GILD\\_COUNTRIES/GILDVENEZUELA/0..contentMDK:20114135%7EmenuPK:262577%7EpagePK:157658%7EpiPK:157731%7EtheSitePK:262571,00.html](http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/LAWANDJUSTICE/GILD/GILD_COUNTRIES/GILDVENEZUELA/0..contentMDK:20114135%7EmenuPK:262577%7EpagePK:157658%7EpiPK:157731%7EtheSitePK:262571,00.html) (Visited on 2 May 2005).

- A bankruptcy proceeding can be suspended or terminated if the unanimity of the creditors decide so, and request it to the Court.

- In the legislation, there is not such thing like extrajudicial reorganization agreements; however, those agreements can be reached by informal agreements between the creditors and the debtor, without any judicial intervention, which are given formality and made enforceable by a Notarial deed.

To avoid discussing specific legal technicalities and formalities described in the Civil Code and other provisions, I will not give specific explanations (subsections) about the insolvency and moratorium relief procedure. In my point of view, with the general characteristics described above is enough. In the next subsection I will give some details about cross border insolvency.

## **5.2. INTERNATIONAL INSOLVENCY ISSUES:**

There aren't provisions regarding cross border insolvency in the Venezuelan legislation, neither the UNCITRAL model law has been adopted until the moment<sup>30</sup>.

The only provision regarding cross border insolvency is related to the presence of foreign creditors not domiciled in the country when proceedings are opened, to which the legislation is favorable in the sense that it allows to this creditors to present to the process even after six (6) months after the Creditors' General meeting is convoked by the Court, without losing their rights.

The recognition of foreign judicial decisions is made according to the proceeding of exequatur, described in the national legislation, and in some cases referred to the parties of the Bustamante Code to which Venezuela is a party.

However, according to the national legislation, if there are assets in the territory, proceedings to liquidate such assets have to be opened in Venezuelan Courts, especially in the case of real estate and assets subject to registration in a public registry.

## **SECTION 6. COSTA RICA:**

### **6.1. GENERAL REMARKS:**

The history of Costa Rica is one of success, due to its economic and political situation, in fact according to the World Economic Outlook<sup>31</sup>, is one of the most successful countries

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<sup>30</sup> Please refer to footnotes No. 17, 19.

in economic terms in the region. Since the 19<sup>th</sup> century only has passed by 2 periods of violence, and its stability in the region is outstanding. Also, its statute of neutrality in international relations has something to do with its success.

Next I will describe some characteristics<sup>32</sup> of its insolvency system:

- The insolvency law in Costa Rica is contained in the Civil Code, Commercial Code and the Code of Civil Procedure. The Costa Rican insolvency legislation differentiates from the traders and non traders, as well as natural and legal persons. There are also special laws related to some institutions, like financial institutions.

- The procedure of reorganization in Costa Rica is mentioned in the Code of Civil Procedure, as reformed by the Law 7643 of 1996, and is called Process of Administration and Reorganization with Judicial Intervention (Proceso de Administración y Reorganización con Intervención Judicial).

- The competent Court for insolvency proceedings is the Civil Court where the debtor has its main place of business. In addition, the Court dealing with the proceeding will deal also, with all the executions that at the moment of opening of proceedings were opened (attraction forum).

- The request for opening a reorganization proceeding has to be presented by the debtor or the creditors.

- In the reorganization proceeding, the Court appoints an interventor, a representative of the employees and two (2) debtors to represent the interest of all the debtors, conforming a Committee which supervises the administrators, and the functioning of the debtor. The Creditors' General Assembly is not mentioned in the Law.

- The creditors don't vote for the adoption of the reorganization plan, they can only give their views.

- In a bankruptcy proceeding the debtor is disempowered from the management of his assets.

- To file for a liquidation proceeding, the creditor must prove the cessation of payment of a credit (consisting of a determinable amount of money and that it is due); in addition, there are other circumstances to file a bankruptcy proceeding, like: the disappearance of

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<sup>31</sup> Table 6(concluded). "World Economic Outlook: Statistical Appendix -- April 2005". Pag. 211. <http://www.imf.org/external/pubs/ft/weo/2005/01/pdf/statappx.pdf> (Visited on 2 May 2005).

<sup>32</sup> Based on: "Costa Rica: Creditor Rights and Insolvency Systems". Vicente Lines – F.A. Arias & Muñoz. Latin American Insolvency Forum – World Bank 2004. <http://www4.worldbank.org/legal/fila/fila2004Papers/Costa%20Rica%20-%20English.pdf> (Visited on 2 May 2005).

the manager of the business, unfair closure of place of business, total assignment of the debtor's assets or fraud.

- There are not administrative or regulatory bodies in Costa Rica that control the administrators or liquidators.

Now, to avoid explaining provisions of the Civil, Commercial and Procedural Codes of Costa Rica indirectly related to the insolvency proceedings, I consider enough the explanation of the main characteristics mentioned here. Next I will explain aspects of cross border insolvency in Costa Rica.

## **6.2. INTERNATIONAL INSOLVENCY ISSUES:**

According to Costa Rican legislation, the foreign and local creditors are equal in many ways, starting with the formalities to file petitions and others. However, the discrimination, and therefore protection of local creditors comes at the moment of the payment of credits, where the creditors (foreign or national) with domicile, branch or agency in the country are paid first; so, if they don't have, foreign creditors will have to wait until the other creditors are paid.

The legislation is considered as following the territoriality principle, because the foreign procedures are not recognized in Costa Rica, and the judicial decisions, to be recognized have to pass by the procedure of exequatur. In addition, Costa Rica is a party of the Bustamante Code, so the procedures laid down in the Code will be applicable between Costa Rica and the other parties of such Code.

The branches or agencies in the country can be independently be declared bankrupt of the principal foreign company, and if the principal foreign company is declared bankrupt, the branches or agencies can be declared bankrupt under Costa Rican procedures.

The UNCITRAL Model Law has not been adopted to regulate cross border insolvency issues.

## **SECTION 7. MEXICO:**

### **7.1. GENERAL REMARKS:**

For my paper, the position of Mexico is very important. Its economy has shown regular growing<sup>33</sup>, and the fact that is a neighbor of the United States and also part of the NAFTA, give the country a big potential to trade and do business. In the last years

Mexico has been concluding several trade agreements with the EFTA countries, the EU, Israel, Chile and several neighbor countries of Central America.

The openness of the Mexican economy started in 1986 when it joined the GATT (now WTO) and several reforms were made to allow liberalization, like the permission for private ownership of commercial banks, the establishment of an independent and technical central bank, agricultural and investment reforms, competition and antitrust laws, etc.

The previous bankruptcy law was enacted in 1943, with a revision in 1987, and had important weaknesses, like the long duration of insolvency proceedings, the many ambiguities which led to different interpretations and the difficulty to obtain a reorganization of the debtor, due to the difficulty to obtain credits and facilities for the debtor during insolvency proceedings.

A new bankruptcy law was enacted on May 12, 2000, in force today, and which I am going to comment briefly here. The new law was enacted thinking in correcting the weaknesses of the former law, due to the new economic and trade realities, especially to obtain better results in reorganization proceedings, with a predictable, transparent and equitable insolvency system.

Next, I will describe some important characteristics of the Mexican insolvency proceedings<sup>34</sup>:

- Mexico is a federal State; Bankruptcy law is a federal matter, so it is governed by federal laws.

- Traders (natural or legal persons) are governed by the law enacted on May 12, 2000 on bankruptcy proceedings. Other natural or legal persons considered as non traders are governed by the rules of the civil insolvency (concurso civil), contained in the Civil Code of the State of the domicile of the debtor, which is the one that is competent to deal with the proceeding. Other laws and parts of the law of May 12, 2000 regulate insolvency proceedings of special institutions, like of the financial sector, of businesses operating under concession of the government, etc.

- The new bankruptcy law states a unique insolvency proceeding called commercial insolvency declaration, which is composed of two (2) stages: conciliation and liquidation.

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<sup>33</sup> Table 6(concluded). "World Economic Outlook: Statistical Appendix -- April 2005". Pag. 211. <http://www.imf.org/external/pubs/ft/weo/2005/01/pdf/statappx.pdf> (Visited on 2 May 2005).

<sup>34</sup> "The new Mexican Law on Commercial Insolvency". Oscós Abogados. Mexico City, Mexico. 2001. [http://www.iiiglobal.org/country/mexico/mex\\_insolv.pdf](http://www.iiiglobal.org/country/mexico/mex_insolv.pdf) (Visited on 2 May 2005).

In the conciliation stage is tried to achieve a reorganization plan; if no plan is achieved, the liquidation stage proceeds.

- The new law eliminates creditors' meetings for claims recognition and approval of reorganization plan.
- The petition to initiate an insolvency proceeding can be filed by the debtor or by a creditor or creditors, and also by the Attorney General.
- The competent Court to deal with insolvency proceedings is the Federal District Court of the domicile of the Debtor.
- The requirement to initiate an insolvency is to have ceased payments of due debts of at least two (2) or more creditors, debts with more than thirty (30) days due, representing more than 30% of the debtor's obligations and that the debtor doesn't have assets to pay at least the 85% of his due obligations.
- All the assets of the debtor, once the bankruptcy is declared by the Court, continue being administered by the debtor, if the proceeding enters into the liquidation stage, the debtor is disempowered of his assets, which pass to be managed by a trustee. The handling of assets is through (at least on paper) the Mexican Court, wherever they are located.
- Arbitration and Court proceedings in course before the petition for insolvency is filed are not joined or accumulated to the insolvency proceeding.
- All claims in insolvency proceedings are denominated in Units of Investment (Unidades de Inversion – UDIS). The conversion to these units is made for purposes of indexing commercial debts, and by that way determining the amount of the debts, and determining the voting participation of the creditors.
- The law created the Federal Institute of Insolvency Mercantile Experts, which is an institution auxiliary of the justice, of a technical and independent nature. This Institute appoints trustees (in the case of liquidation) or conciliators (in the case of conciliation/reorganization proceedings).

For more details about the insolvency system in Mexico, please check the Annex V of this paper.

## **7.2. INTERNATIONAL INSOLVENCY ISSUES:**

Mexico has adopted<sup>35</sup> in its entirety the UNCITRAL Model Law on Cross Border Insolvency, as part of the insolvency law of May 12, 2000.

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<sup>35</sup> "Mexico's International Bankruptcy Provisions". Markowitz & Fernandez. <http://www.iiiglobal.org/country/mexico/bankruptcy.pdf> (Visited on 2 May 2005).

## CHAPTER IV:

### CHALLENGES RELATED TO INSOLVENCY IN LATIN AMERICA

In the first chapter I described the new economic and trade realities, with an approach to the Latin American countries. My purpose with this description, which at first sight is not related to the insolvency regimes; was to describe how the new economic and trade realities have affected the Latin American countries to a point that many of them have started to change their legislative framework to adopt it to an environment of open economy; this new approach has influenced directly the insolvency regimes: by creating special regimes (in every sense) to controlled and key sectors of the economy, by creating more flexible bankruptcy proceedings giving liquidators and receivers a wider margin of action, by in many cases creating inexistent reorganization procedures to allow survival of viable enterprises, and by taking a protectionist approach directed to the companies, the entrepreneurs and the society in general to achieve the goals of healthy economies with improvement of living standards for the population.

In the second and third chapters I have mentioned the development of several Latin American insolvency regimes to the actual moments, giving also a description of the key points of those regimes.

However, there are still challenges to overcome. In this fourth chapter, I will describe those challenges both in cross border and domestic insolvency regimes, based on documents issued by the United Nations, the International Monetary Fund, the World Bank and other institutions; and, I will give some suggestions to be adopted by those countries in order to achieve a successful insolvency regime. But first, in the first section of this chapter, I will give an outline of the different theoretical modern approaches towards insolvency, in order to understand what follows.

#### **SECTION 1. BRIEF THEORETICAL APPROACH:**

Insolvency law has many legal profiles<sup>36</sup>, which leads to think that there is a double profile of this specific system: a substantive and a procedural profile.

The procedural profile aims to establish a common procedure, to order the recognition and execution of the different kinds of credits and creditors, and in that way avoid individual actions, resulting in a collective action, in which it's possible to reorganize or to liquidate the debtor. The lack of this profile would lead to inequality of some creditors over others (procedural fast creditors over slow procedural creditors), the debtor also would be compelled to dissolve or disappear his patrimony to avoid the liquidation, the social objectives of a market chain would be lost because of the desires of creditors to

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<sup>36</sup> Based on the book: "Derecho concursal internacional". Alfonso-Luis Calvo Caravaca y Javier Carrascosa González. Madrid: Colex. 2004.

split the debtor's assets to pay his credits (affecting producers, suppliers, consumers, economy in general).

The substantive profile aims to establish a way and a measure in which the creditors would satisfy their credits. The idea is to protect the rights acquired outside the insolvency procedure; ensuring to creditors that their credits have a high probability of being recovered. In this way, not only the creditors or debtors are satisfied, but also other parties not directly related to the insolvency process, due to the economic security that it gives.

Related to the cross border insolvency, it deals with two (2) characteristics: 1) internationalization of the economic activity, even easier with the creation of economic blocs and free trade or investment agreements, and 2) diversity of countries' legislations, with the differences in the main issues to open an insolvency proceeding, the quality of the debtors to which the insolvency procedure is applicable, the types of proceedings and functions of the insolvency proceeding. The legal problems arising from this issue are not present in the domestic cases, which makes cross border insolvency a more complex subject. Indeed, the lack of an adequate legislation on this subject, leads to several problems, like the lack of legal security, which in turn could lead to legal problems to solve in cross border insolvency (problems of international private law as competence, jurisdiction and cooperation), the disincentive to the flow of foreign investment and the flow of capital, and the inequality of foreign creditors over the national creditors. Moreover, it could lead to the figure of the "forum shopping", in which the debtors could seek for weak insolvency regimes to translate his patrimony and avoid execution or even violate creditors' rights.

The globalization of the economy, and in order to avoid the problems that it creates, including the ones mentioned above, is leading to the different countries to adopt a component dealing with cross border insolvency. This component in my opinion has to be simple and flexible to avoid elevated costs than could contravene the objectives of the insolvency regimes, dealing effectively with the competence of the Courts, the *lex concursus*, and the extraterritorial effectiveness of the judicial decisions.

In this sense, the cross border insolvency regimes have taken two directions: one leading to territoriality, and the other leading to universality. There are, in addition, mixed regimes, which are the secondary insolvency proceedings and the independent insolvency proceedings.

The universality regime has the following characteristics: 1) the Courts of a State where the debtor has his domicile or his center of main interest have the competence to open insolvency proceedings. 2) The *lex concursus* is the law of the State of opening of the proceedings. 3) The *lex concursus* affects all the assets of the debtor, no matter where those assets are located. 4) All the creditors of the debtor have to file their claims in the Court with the aforementioned competence (so there won't be distinction between foreign

and local creditors, thus, no discrimination between creditors – par condition creditorum). 5) Judicial decisions of the competent Court are effective in every place where the debtor has assets.

The territoriality regime has the following characteristics: 1) the competent Court is not only one but many, depending of the countries where the debtor has assets. 2) The lex concursus is not one, but as many as there are competent Courts in different countries, so, each procedure is governed by its own lex concursus. 3) The creditors can only file their claims in one of the insolvency proceeding. 4) Judicial decisions of the competent Courts are effective only in the territory of the State where they belong.

The secondary insolvency proceedings refer to: 1) the opening of a main insolvency proceeding in the domicile or center of main interest of the debtor, to which can file claims all creditors that wish so, and the decisions of the Court are valid abroad. 2) The opening of a main proceeding doesn't prevent to open territorial insolvency proceedings where the debtor has some assets, such proceedings are parallel and subordinated to the main proceeding, and are limited to the assets in the territory of that State.

The independent insolvency proceedings refer to: when it's impossible or not necessary to open insolvency proceedings for all the structure of the debtor, but only to a part, or even, where there is only a permanent establishment where the debtor has entered in bankruptcy.

## **SECTION 2. CHALLENGES IN TERMS OF CROSS BORDER INSOLVENCY:**

As I will mention, the cross border insolvency systems in Latin America are not well developed, most of them are based in a territorialist approach and only open to a more universalistic approach (or better, a modified territorialism) in a few bilateral and multilateral cases. Moreover, many of those systems are, for means of collaboration and communication between foreign and domestic Courts, based on old provisions of substantive and procedural Codes<sup>37</sup> that, if even is true that those provisions work, are not in accordance with the modern world and, more specific, with the functioning of modern insolvencies. It is important then, for Latin American countries, to overcome those challenges in order to have effective cross border insolvency regimes and therefore, be competitive in the modern world.

In terms of cross border insolvency, it's worth to mention the efforts in the framework of the American Law Institute, the United Nations Commission on International Trade Law (UNCITRAL), and the example of the European Union with the Regulation 1346/2000. I

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<sup>37</sup> Specific examples are letters rogatory, exequatur, and application of the doctrine of comity.

must clarify before continuing that my objective in this paper is not to make an exhaustive analysis of the different alternatives<sup>38</sup>.

1) In first term, with the adoption of the Transnational Insolvency Project<sup>39</sup> (2001), under the auspices of the American Law Institute (ALI), and following the signature of the NAFTA between the USA, Canada and Mexico. This project, consisting of 17 guidelines, resulted<sup>40</sup> in an authoritative summary of insolvency laws and practices of each country and a set of cooperative procedures for use in the private and public sector. This project, is worth to mention, is not hard law, neither an intent to harmonize the laws of the different countries, but an initiative to optimize coordination and cooperation in cross border insolvencies, with protocols limited to legal entities and commercial matters, that can be used by private parties and Courts without the need of legislation, to ensure the maximum benefit for stakeholders of a financially troubled enterprise.

This project aims to solve problems of judicial independence, proper procedures and credibility which arise in a cross border environment.

2) The Cross Border Insolvency Concordat (1996), emanated from the Committee J of the International Bar Association<sup>41</sup>, is another example to follow; this document aims to state general principles to guide and assist participants in cross border insolvencies, not to substitute for treaties or statutes, and has a universalistic tendency. Consisting of ten (10) principles, those states for the administration by one main forum of insolvency proceedings, transparency and collaboration in the cross border proceedings, non discrimination of creditors, and respect for the right of defense.

3) The EU Insolvency Regulation<sup>42</sup> (1346/2000) is another example worth following; although it has a universalistic approach (universal effect of *lex concursus*, except where there are rights in rem or immovable property, contracts of employment, etc), very open, with a view of the principle of “mutual trust” between the countries (and its Courts) forming the European Union. The Regulation contains an ingredient of non discrimination between domestic and foreign creditors (even with right of foreign tax authorities to lodge claims in a non domestic proceeding), and cooperation and

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<sup>38</sup> Based on: “Procedural Incrementalism: A Model for International Bankruptcy”. John Pottow. 2005.

<http://www.law.umich.edu/CENTERSANDPROGRAMS/OLIN/abstracts/discussionpapers/2005/05-001pottow.pdf> (Visited on 13 June 2005).

<sup>39</sup> The full text of the Transnational Insolvency Project (ALI – TIP) can be consulted in: <http://www.iiiglobal.org/international/projects/ali.pdf> (Visited on 10 June 2005).

<sup>40</sup> Based on: “Cross Border Insolvency Procedure between the United States, Mexico and Canada: the Transnational Insolvency Project”. Muzi Kubeka. Griffin’s View on International and Comparative Law, Volume 4, Number 2. 2003. <http://www.rechten.vu.nl/dbfilestream.asp?id=1195> (Visited on 2 May 2005).

<sup>41</sup> The full text of the cross border insolvency concordat can be consulted in: <http://www.iiiglobal.org/international/projects/concordat.pdf> (Visited on 13 June 2005).

<sup>42</sup> The full text of the EU Insolvency Regulation 1346/2000 can be consulted in: <http://europa.eu.int/eur-lex/lex/LexUriServ/LexUriServ.do?uri=CELEX:32000R1346:EN:HTML> (Visited on 13 June 2005).

communication between liquidators, differencing between main proceedings, secondary and independent insolvency proceedings, stating the powers of liquidators, etc<sup>43</sup>. It is important to remember that, as a Regulation, has general application, it is binding in its entirety and directly applicable in all Member States<sup>44</sup>, except for Denmark.

By definition, this Regulation is the ideal point to reach, although it has a limited scope (only in intra community proceedings), this Regulation shows the application of universality as ideal and states the communication and collaboration of foreign liquidators in its entirety, with even far reaching effects than the ones of the UNCITRAL Model Law; it is an example of how the new economic and trade realities can affect a group of countries. The provisions of this Regulation could be an example to follow in Latin American countries, when those reach a higher level of integration (in a bilateral or multilateral level).

4) Another example to follow by the Latin American countries is the adoption of the provisions stated in the UNCITRAL Model Law on Cross Border Insolvency<sup>45</sup> (1997). A flexible and very important instrument, emanated from a quasi legislative body, and which takes into consideration many previous documents, protocols, treaties and conventions from many different geographic locations and the different systems (universal and territorial), that aims to solve problems arising especially when the debtor has assets in several States, or there are creditors that are not from the State where insolvency proceedings are taking place. In more specific terms<sup>46</sup>, aims to allow recognition of foreign insolvency proceedings in a national Court or vice versa, the coordination of insolvency procedures between 2 or more States, and the participation of foreign creditors in local insolvency proceedings, clarifies the powers of liquidators or receivers to act in foreign procedures or and for foreign liquidators or receivers, its powers and recognition in domestic proceedings, simplifies requirements to access insolvency proceedings, establish the adoption of interim measures while the recognition of a foreign proceeding is accepted, establish also that local Courts can refuse to take some action based in foreign proceedings if its contrary to its public policy, etc.

In short terms, the success of the Model Law lies in that it advanced in universalism in a way that does not conflict with territorial jurisdictions<sup>47</sup>, mainly by setting rules of cooperation, communication<sup>48</sup> and antidiscrimination<sup>49</sup>.

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<sup>43</sup> To consult a full analysis of the Regulation 1346/2000/EC check: “The European Union Insolvency Regulation. An Overview with Trans-Atlantic Elaborations”. Bob Wessels. [http://www.iiiglobal.org/country/european\\_union/Norton03Wessels.pdf](http://www.iiiglobal.org/country/european_union/Norton03Wessels.pdf) (Visited on 13 June 2005).

<sup>44</sup> Art. 249 Par. 2 EC Treaty.

<sup>45</sup> The full text of the UNCITRAL Model Law on Cross Border Insolvency can be consulted in: <http://www.uncitral.org/english/texts/insolven/insolvency.htm> (Visited on 10 June 2005).

<sup>46</sup> To obtain a more detailed description of the Model Law, please check: “UNCITRAL Model Law on Cross Border Insolvency with Guide to Enactment”. [http://www.iiiglobal.org/organizations/uncitral/model\\_law.pdf](http://www.iiiglobal.org/organizations/uncitral/model_law.pdf) (Visited on 10 June 2005).

<sup>47</sup> See Arts. 6 (refusal to act of a Court based in public policy), 21 (2) (Court can refuse to entrust assets in a State to a foreign representative if considers that interest of creditors in this

To fall within the scope of the provisions of the Model Law, the proceeding has to be considered an insolvency proceeding, characteristics which I have already described in previous chapters of this paper (based in an insolvency law, with collective involvement of creditors, control and supervision of assets and affairs of the debtor by a Court, etc).

Without any doubt, in the short/medium term, the UNCITRAL Model Law on Cross Border Insolvency is the solution for Latin American countries to have an effective cross border insolvency regime. The previous argument is supported, not only in the fact that the Model law is a flexible instrument which permits the adoption with changes, reservations and interpretations of the provisions, but also of the fact of being emanated of a serious institution with previous debates and studies, and also that took into consideration previous treaties and conventions between Latin American countries, and others.

### **SECTION 3. CHALLENGES IN TERMS OF DOMESTIC INSOLVENCY REGIMES:**

Most of the modern insolvency systems, not only in Latin America, but all over the world, are focused on some key objectives: 1) allocation of risks between participants in a predictable, equitable, and transparent way; 2) maximize the value of the insolvent firm to benefit not only the interested parties, but the economy in general.

#### **3.1. CHALLENGES TO OVERCOME:**

As I mentioned before, in Latin America most of the insolvency regimes are aimed in protecting the enterprises to, by that way, protect employment; another primary objective of insolvency regimes is to reduce the impact of bankruptcies in the private sector debt, which is reflected in the national economy. Those goals, most of the times have a cost: a weak creditor protection. By that way, it can be seen that many times, creditors can suffer loses in recovering their credits, and those loses can be significant (not only in economic terms) if it is taken into consideration that many of those creditors are active participants in the economy of the countries (banks, institutional investors, natural persons, to name the most relevant ones). The challenge then, from the Latin American perspective, is to strike the balance between protection of the debtor and protection of creditors.

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State is not well protected), 28, 29 (preeminence of local proceedings even over foreign main proceedings in some cases).

<sup>48</sup> See Arts. 25, 26, 27, 30 of the UNCITRAL Model Law on Cross Border Insolvency.

<sup>49</sup> See Arts. 9, 12, 13, 24 *ibid*.

In addition, many authors agree that most of the insolvency systems in Latin America are<sup>50</sup>:

1) “*(R)igid, formalistic and old*”. Moreover, in the same document (dated 1999), the authors quote the specific examples of Mexico and Brazil, which it is to remember, as mentioned, have enacted recently, new insolvency laws (year 2000 and 2005, respectively), no wonder that in response to such and other critics.

2) With a “*high degree of judicial discretion*”. Where the Judge has the last word. It is important to mention that actually, Judges (and insolvency authorities) have to take their decisions based in arguments and in the advice of the trustee, liquidator or receiver. Those decisions, in a later stage can be reviewed. In addition, in recent reforms, as I have already mentioned, many critical decisions are taken not by the Court, but by the Creditors’ Committee or Creditors’ General Assembly.

3) “*Corruption*”. In the sense that a few key parties control the proceedings, receiving favourable treatment. This kind of behaviors is mostly applicable to the graduation of credits and the adoption of excessive creditors’ privileges. In my view, this a problem unique to Latin America, but applicable also in other countries, that has been slowing down in recent years due to the restriction on voting rights and the explicit control of insolvency authorities.

4) The absence of a “*Rescue culture*”. This problem is traduced in the lack of enforcements of judgments protecting creditors’ rights and the financial inestability by creditors accepting settlements which do not cover the real costs of the debt; in some countries because of the lack of cohesion and cooperation between the judicial and the public forces, or the level of autonomy between federal and State authority or even the delays in the issuing of judgments because of the congestion and diminution of the size of bureaucracy (consequent with the economic and political model followed by the Latin American countries and the budgetary crisis); but actually, in many of the Latin American countries, because of the lack of budget to finance effective enforcement.

5) Excessive preferences to labor credits. In my opinion, this is not a problem of the States as such, but of the system, and can not be pointed as a problem of Latin America, due that the same protection is available in other developed countries (with a social model).

### **3.2. PROPOSED SOLUTIONS:**

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<sup>50</sup> Based on: “Reforming Insolvency Systems in Latin America”. Malcolm Rowat & Jose Astirraga. World Bank Note No. 187. World Bank. 1999. <http://rru.worldbank.org/Documents/PublicPolicyJournal/187rowat.pdf> (Visited on 13 June 2005).

The aforementioned authors, in a more formal document under the auspices of the World Bank<sup>51</sup>, as solutions for those problems propose:

1) Judicial reform to train the Judges, create specialized bankruptcy Courts, and reduce the time of proceedings. In addition, these reforms should be accompanied by legislative reforms in other key sectors touching bankruptcy, like guarantees, financial sector (including the capital market), social security and labor, exchange rate policy, etc., to allow more flexibility in reorganizations as well as a better flow of capital, necessary for to reach a successful, bankruptcy or reorganization, depending of the case.

The document, in my point of view, stresses very well the urgent needs of the Courts to be more efficient, needs which the World Bank is working to enhance. I quote: *“The needs range from computer equipment and software to track cases and rulings, to additional staff, to training for existing staff, to basic office equipment, to know-how for better management of filings and case files, and even efficiency studies to determine how to streamline the flow of paper”*<sup>52</sup>.

Most of the Judges don't know basic business notions necessary for the correct handling of insolvency cases, like the calculation of interests, credit terms, foreign exchange, etc. Those concepts, albeit should not be qualifications to become a Judge, should be focused in training programs, especially for the Judges with jurisdiction and competence where insolvency cases are handled often.

As a solution for those problems especially related to the judiciary, many Latin American countries have opted to create and enhance the functioning of “Escuelas de Magistratura” (“Magistrate School” or “Judgeship School”), or with cleverer structural reforms like leaving those technical aspects to specialized trusted judicial auxiliaries (mainly the same trustees, receivers, liquidators), or taking out of the jurisdiction of the judiciary the insolvency cases, with the creation of administrative, technical and independent bodies like the “Superintendencias” (Superintendences) with a function to handle some of the issues arising in insolvency procedures and a surveillance function over the liquidators, trustees, receivers, and other parties which gives more flexibility to the system.

In the other hand, the surveillance of enterprises and economic players has been enhanced to allow a framework controlled by laws and details and interpretations to other more permanent and technical institutions or persons.

These same solutions can be used to solve the long delay in proceedings that most of the times can mean the difference between life and death of a company or create deeper problems like the denegation of justice.

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<sup>51</sup> “Latin American Insolvency Systems: A Comparative Assessment”. World Bank Technical Paper No. 433. World Bank. 1999. [http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/1999/06/04/000094946\\_99042010294995/Rendered/PDF/multi\\_page.pdf](http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/1999/06/04/000094946_99042010294995/Rendered/PDF/multi_page.pdf) (Visited on 13 June 2005).

<sup>52</sup> Ibid. page 14.

2) Separate criminal and bankruptcy statutes. As I have mentioned when I explained some of the characteristics of insolvency regimes in previous Chapters of this paper, some Latin American countries incorporate provisions of criminal law in their insolvency regimes. In my point of view, I can not attack directly those ways to deal with provisions, even more if it's taken into account that such ways vary depending of the domestic circumstances of each country; what I can say, is that the practice and several documents promoting judicial reform have shown that what such a practice does is to make more complicated insolvency regimes. The solution to this problem should be aimed in leaving separated those criminal provisions out of the insolvency regime, by either incorporating to the criminal Codes or provisions of the countries, or by eliminating such detailed provisions leaving only key factors and the details to be handled by the general principles/provisions and procedures of criminal law (like the definition and gradation of criminal liability and the factors of aggravation and relief), which in time can be focalized by judicial interpretation and doctrine, as auxiliary criteria of the law.

3) A more frontal fight against insolvency corruption. As I mentioned, corruption is not a problem only of Latin American countries<sup>53</sup>, and should be faced not in a specific way against insolvency proceedings, but in general to all aspects of the society, by giving a higher rank to this fight. The fight against corruption should start not in the insolvency proceedings, but in the same law of the country, and for the specific case in the domestic company law, by the adoption of Codes of Good Governance, which allow more transparency in the decision making of the companies, for example. Also a good point would be to allow the same creditors to create an Ethics Committee which would be able to denounce possible corrupt activities, not only in the proceedings but also in the normal activities of the company and which would be contrary to the interest of the creditors putting in risk the recovery of the company or the patrimony of the company as a mass to be liquidated.

In the other hand, the fight against corruption in insolvency proceedings itself, should be focused in the transparency in decision making, of all the parties related, and the elimination of possible “cartels” of creditors, by pluralizing the decision making process (a kind of “healthy restriction of voting rights”). Another good point would be to enhance the actions that look for the nullification of operations and recovery of assets, sold fraudulently or by any other means contrary to the rights of creditors, as example would be to enhance alternate dispute resolution methods.

Again here, the activity of an independent, technical body with functions of surveillance (like the Superintendences) would be of great help. Anyway, the key aspect is to achieve a simple but effective system preventing the duplicity of functions, to avoid blocking the insolvency proceedings.

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<sup>53</sup> See cases: ENRON, WorldCom, Parmalat, etc. In the USA and Italy, which were a warning bell and gave rise to the enactment of the Sarbanes-Oxley Act in the USA.

4) Enhance the transparency in handling and communicating information. I will give an explanation to this point as part of another points of this paper, to avoid duplication of arguments, due that I consider that the present point is closely and directly related to other important points which I will elaborate.

5) Achieve more specific interpretation of the provisions of insolvency regimes and provide “escape valves” to avoid strict mandatory liquidations. Also, to enhance flexibility in reorganization proceedings.

It is important to mention that such goals can be achieved by promoting insolvency regimes that allow flexible interpretation, either by the judiciary or by independent, technical bodies. The rigid insolvency regimes are problematic because the laws enacted by the legislative tend to have many delays or take too long to be enacted. The modern tendency is to have laws with a legal framework (including in insolvency) and the development of details of those laws by administrative acts, enacted under the authority of independent, technical bodies, and interpretations by the judiciary, as well as its Constitutional control.

In addition, the flexibility in reorganization can also be achieved by providing methods to sell a percentage of participation in reorganization proceedings, as a way, to allow a viable enterprise, to let go stakeholders with no trust in the recovery of it. And also, the possibility of prepackaged accords is possible, and the enhancing of the alternate dispute resolution methods<sup>54</sup> to allow the settling of disputes between stakeholders and avoiding the mandatory liquidation or proceed to unnecessary reorganization proceedings, which could be interpreted as that “the remedy could be worse than the illness” or be used by the enterprises to defraud creditors by using the advantageous reorganization provisions (example, stay of proceedings, etc) or legal holes (example, a broad and inaccurate interpretation of the term cessation of payments).

Other more financial solutions would be to enhance provisions to allow payments “out of schedule”, because many times the financial situation of an enterprise doesn’t depend only of internal factors, but also of external, also the conversion of debt into equity or capital restructuring, escape valves in execution contracts (to liquidate or terminate the unprofitable ones), and allow set offs to cancel cross debts between creditors and the debtor, but giving sufficient guarantees to avoid or nullify by that method fraud to the other creditors. The reorganization agreements should represent reasonable conditions for a viable enterprise to recover, but can not put into a square the enterprises as to be jailed on it. Modern management doctrine has shown that many companies in crisis have found remedies in innovative solutions!<sup>55</sup>

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<sup>54</sup> As an example, in Colombia the “Superintendence of Companies” encourages the use of conciliation and arbitration as methods to settle disputes between stakeholders, with very good results.

<sup>55</sup> “If It Ain't Broke...Break It! and Other Unconventional Wisdom for a Changing Business World”. Robert J. Kriegel with Louis Patler. Publisher: Little Brown & Co.

A last important aspect in this point is to provide or state clearly insolvency regimes for groups of companies, holdings and part of those companies, which would allow flexibility and avoid a financial crisis in whole conglomerates. Popular wisdom takes a good role here: if an arm is rotten, is better to cut it before the disease attacks the whole body!

Without any more comments, a key factor in this point is to promote in every country the “rescue culture”, which can only be achieved by taking global measures to create TRUST in the whole system.

6) Adopt cross border insolvency regimes. With especial emphasis on the UNCITRAL Model Law on Cross Border Insolvency.

As a part of its effort to promote the adoption of efficient insolvency regimes in Latin America, the World Bank released in April 2001 the document “Principles and Guidelines for Effective Insolvency and Creditor Rights Systems”<sup>56</sup> (hereinafter “document”). This document, which was product of consultations between several international institutions and other private and public sector officials, aims to be useful as guide for the enactment of efficient insolvency regimes, containing international best practices in the design of regimes of creditors’ rights and insolvency; and is directed to the whole international community, and not especially to Latin America.

The document offers principles referred to: creditor rights (principles 1-5), insolvency systems (principles 6-16), corporate rehabilitation (principles 17-24), informal corporate workouts (principles 25-26), and implementation of insolvency regimes (principles 27-35).

In those principles, the document stresses the importance of effective enforcement of rights, effective methods of registration of rights, the integration of insolvency systems with the whole legal framework, responding to domestic and international needs, also to establish an effective framework of directors’ liabilities, the scope of both insolvency and reorganization proceedings, etc. Mainly by adopting all the key points mentioned in the documents quoted in this paper.

In addition, the International Monetary Fund has incorporated in its agreements with developing countries (based in the requirements of conditionality)<sup>57</sup>, the improvement of its insolvency regimes, because of the impact that they have in the economic and financial system. Its main conclusions were as follows:

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<sup>56</sup> The full text of this document can be downloaded in the following URL: [http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2004/11/16/000160016\\_20041116125959/Rendered/PDF/306470v.20DC200100008.Rev1.pdf](http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2004/11/16/000160016_20041116125959/Rendered/PDF/306470v.20DC200100008.Rev1.pdf)

<sup>57</sup> Based on: - “Promoting Orderly and Effective Insolvency Procedures”. Sean Hagan. Magazine Finance and Development, March 2000, Volume 37, Number 1. Published by the IMF. <http://www.imf.org/external/pubs/ft/fandd/2000/03/hagan.htm>

1) The adoption of an efficient legal framework for insolvency proceedings is necessary, but countries can adopt special regimes for highly regulated entities or natural persons. The fact that an enterprise is State owned is not an excuse to exclude it from a general insolvency regime.

2) The petitions for commencing insolvency proceedings should be filled either by a creditor or by the debtor, and the main criteria to commence insolvency proceedings should be the general cessation of payments. In addition, the use of penalties or incentives should be stated in order to avoid the late commencement of insolvency proceedings or to promote incentives for early commencement.

3) Upon the commencement of a liquidation proceeding, the debtor should be disempowered of his assets. The paper of interim measures is important and of the stay of proceedings to protect the assets of being distributed outside the liquidation proceeding; in addition, the stay of proceedings should be limited in time for secured creditors.

4) Mechanisms to improve powers of liquidators to recover transferred assets with the intention to defraud creditors should be improved, and create a “suspect period” where transactions in such period prior to filing of insolvency should be under especial surveillance, as well as improving surveillance of transactions with insiders.

5) The powers of liquidator / administrator, trustee, receiver should include the termination or continuation of contracts, depending of the profitability of those and the effect over other contractual relations. Such powers should be limited regarding some types of contracts, like financial and personal services contracts.

6) A right to set off should be protected and encouraged.

7) Liquidation should be efficient. In this terms, public auctions and private sales should be allowed, but with the sufficient transparency and communication of information, and taking into account the maximization of the value of the assets.

8) Secured creditors and administrative expenses should have priority in the gradation of credits. In addition, the proceeds of sale of encumbered assets should serve to pay creditors guaranteed with those. Statutory privileges should be limited and discrimination between foreign and domestic creditors should not exist.

9) The law should provide a mechanism of conversion from reorganization proceedings to liquidation proceedings, previous requirement of the same debtor, creditors or the Court at its own motion. In addition, the reorganization proceeding should not exceed of a limited and specified period of time.

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- “Orderly and Effective Insolvency Procedures: Key Issues”. Legal Department. IMF. 1999.

10) A stay of proceedings in a reorganization proceeding should be allowed. In addition, the debtor should, in the course of a reorganization proceeding, be allowed to keep control of his assets and management of his enterprise but under close supervision of an independent person/ body.

11) In a reorganization proceeding, the debtor should have the opportunity to prepare a reorganization plan, if after a limited period the debtor has not presented a plan, the opportunity to do it should be given to the receiver, trustee or administrator, or to the creditors.

12) The reorganization plan should be binding upon all creditors, secured and unsecured upon the recognition and respect of their rights and of all the dissenting creditors. However, if the creditors are voting and separated according to different economic interests, discretion should be applied to avoid creating “cartels” and making binding plans voted only for one or a few classes of creditors, to avoid also the violation of rights of different classes of creditors.

13) The Court should only reject a reorganization plan in limited and / or exceptional circumstances, even more if it has already been approved by the administrator, trustee, receiver and the creditors.

14) Obtention of financing should be allowed under reorganization proceedings, taking into account the position of recognized credits.

15) Reorganization should be efficient. Therefore, the approval and existence of pre packaged reorganization plans should be allowed, and Courts should be able to approve those plans even before commencing of reorganization proceedings.

16) The formation of Creditors’ Committees should be permitted. Moreover, the liquidators / administrators, trustees, receivers should be appointed by a Court and under pre existent and high professional qualifications.

17) The Courts should act with predictability. Therefore, the law should provide how Courts can exercise their discretion. In addition, the creation of specialized bankruptcy Courts should be promoted.

18) Once more, the adoption of the UNCITRAL Model Law on Cross Border Insolvency is encouraged to deal with issues of communication and cooperation in cross border insolvencies.

Many of those conclusions are shared by other institutions<sup>58</sup>, and the World Bank in special is keeping a record<sup>59</sup> and encouraging the development of insolvency law, not only at Latin American level, but worldwide.

I understand that all the aforementioned points seem very long and make this section look complex, but my objective with this is to give a wide point of view of the different positions towards adopting insolvency regimes, and I stress this because as I have mentioned here the view of the World Bank in the quoted document is towards Latin America, and the view of the International Monetary Fund in the quoted document is towards, not only Latin America, but worldwide.

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<sup>58</sup> “The Regulatory Gap: the Cost of Capacity Building”. Peter Joyce. Presented in the World Bank Global Forum on Insolvency Risk Management – Standards and Strategies. Washington DC, 28 – 29 January 2003. The full document can be consulted in: [http://www.insolvencyreg.org/sub\\_publications/docs/Paper%20Gordon%20Johnson%20World%20Bank.doc](http://www.insolvencyreg.org/sub_publications/docs/Paper%20Gordon%20Johnson%20World%20Bank.doc) (Visited on 15 June 2005).

<sup>59</sup> See: - World Bank - Global Insolvency Law Database: <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/LAWANDJUSTICE/GILD/0,,pagePK:181022~theSitePK:215006,00.html> (Visited on 15 June 2005).

- World Bank – Report on the Observance of Standards and Codes: <http://www.worldbank.org/ifa/rosc.html> (Visited on 15 June 2005).

## CONCLUSIONS

In the development of this paper, I have discussed the new economic and trade challenges Latin American countries face, the major points of the insolvency regimes in a selection of these countries, and the efforts of international institutions to promote the adoption of new, modern and improved insolvency regimes not only in this specific geographic location, but worldwide.

The conclusions to be mentioned are that in terms of challenges of the insolvency regimes of Latin American countries facing the new economic and trade realities, yet there is much to advance. Despite many countries have adopted modern insolvency regimes, like in Argentina and Mexico, to name some examples, there are yet many points to overcome, even in those countries. The rigidity and formalities applied in many countries to their insolvency regimes take out many of their good benefits, especially when attaching procedures of insolvency to procedures stated in their Codes, which, although in some cases is good, in others attach the insolvency regimes to rigid, formalistic procedures, and why not? To the same fate than other proceedings not related to insolvency by imposing the same general rules; I mean, that if an insolvency proceeding, as I have mentioned and supported should be handled with celerity, why subject it to the same general procedures of the Codes, in which it should be handled with the same and almost usually incompatible procedures to which other issues are handled, besides, if we interpret the principle of due process and the one of non discrimination in a restrictive way, lacking a specific provision in the law, the insolvency proceeding should be subject to respect an order (be it of entrance, type of procedure, or any other), which in the end would end by denaturalizing it, among other legal considerations.

In answering this research question I agree completely with Mr. Rowat and Mr. Astirraga in their conclusions<sup>60</sup>, especially when they refer to the lack of training of Judges and the lack of specialized bankruptcy Courts. It may be true that the main reason to not introduce it is because of the lack of budget, it is also true that the systems itself are not well prepared in the sense that they leave a big workload to the Courts and Judges and don't delegate to judicial auxiliaries, which may prove to be very helpful in this kind of situations. I repeat again, that if an insolvency system gives a correct background and framework it should not be so complex for Judges or Courts to be really persons with integrity and professional qualifications. The Judge or Court should focus then, in key factors for insolvency proceeding expressly stated in the law, with a high degree of help from the trustee, administrator, liquidator or judicial auxiliary; in that way, avoid many practical problems that could arise by leaving the Courts with a high level of discretion and also, by that way, focus the educational programs for Judges to what the real necessities are (to key factors in insolvency proceedings and even other kind of proceedings, and in doing so, using more effectively the resources from the budget, which are always short for the necessities to be covered).

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<sup>60</sup> Refer to footnote 50.

The fight against corruption is also another factor, although not specifically related to Latin America, because as I mentioned in the respective part of the paper, corruption exists in many countries. The fact is that in this point the fight is to a never end, that is why, it shouldn't be focused only to insolvency proceedings, but to have a general approach, in that way, such programs to fight against corruption could have an effect in time and sustainability. In addition, statutory provisions are need, elevating the economic fines to this kind of behaviors and the punishment for such conducts. By doing so these fines and punishments should take into consideration the quality of the parties (public officers, auxiliaries, or private parties), and the fact that in the moment that an insolvency proceeding is filed the obligations of a company change, from answering to shareholders to answering to stakeholders (creditors, minority shareholders, employees, etc) and in many cases to the society in general (by for example, an obligation to preserve employment or the productive system of a determined place, or even the stability of market conditions – case of highly sensitive economic sectors and companies with a high participation in the market -). The same idea can be directed to separate criminal and insolvency provisions; as I commented for example in the case of Chile, what it does is only adding complexity to something that by itself is already complex. Criminal and other provisions should be separated; the criminal provisions should be managed under the general criminal law of each country, giving wider margin for interpretation and integration into the legal background of each country.

The lack of transparency in handling and communicating information is also a problem in Latin America; this problem can also be directly linked to corruption, increasing the ability and formation of cartels and the lack of flexibility of insolvency proceedings. Although this problem can be characterized for the size, geography and lack of development of communication methods of the Latin American countries, this excuse is not at all satisfactory, because of the fact that many insolvency procedures are dealt with Courts located in urban centers (for the case of the use of the domicile), or in “centers of main interest” with high economic movement; also, the fact that there are many ways of communication to handle information, being the Internet one of the most popular and with high coverage. The Internet then, in my point of view is the solution for this problem, not only because it allows to transmit information in an equal basis, but also because it allows to implement more specific solutions; some Latin American countries, for example have implemented websites (virtual marketplaces) where they can auction or sale insolvency assets or manage creditor' rights in an efficient and transparent way. Another way to improve transparency is to give continuity or adopt Codes of ethics or Codes of Good Governance, which have proven to bring good results in the corporative life.

The fact that insolvency proceedings are mostly dealt by Courts is a problem also, this statement can be linked with the lack of capacity and specialized Courts in the systems. This problem has been solved in many countries by taking out of the competence of the Judiciary the surveillance and handling of the insolvency proceedings, but this solution is

not as effective as one can think, because what it does is to move a problem from one part of the system to another (the problem can not be located in who handles the proceedings, but can be an structural problem of the system) or can rise Constitutional problems by creating a discussion of intervention of one of the branches of the public power over another, or the creation of judiciary functions to an administrative entity.

Without any doubt, the major problem in Latin American countries in terms of insolvency regimes is the lack of effective provisions of cross border insolvency; in this modern world, as I mentioned in this paper, the new economic and trade realities require the effective handling of cross border insolvency regimes. In addition, and as a plus to the adoption of cross border insolvency regimes, the adoption of effective and flexible insolvency regimes for branches or groups of companies is necessary (both domestic and cross border), is not a secret that the big conglomerates are organized as holdings, and the adoption would add simplicity to insolvency proceedings that statutory provisions make more complex and that at the end would have the same results. In this case, combined with effective domestic provisions, the adoption of the UNCITRAL Model Law on Cross Border Insolvency is a great opportunity to Latin American countries.

In addition, in the domestic legislative framework, Latin American countries still have to improve in solutions to avoid mandatory liquidation of viable enterprises; this can be possible by adopting the possibility to have prepackaged restructuration plans (in the form for example of solemn contracts between stakeholders of an enterprise), which can improve the possibilities of recovery of an enterprise by allowing to reduce the unpredictability and traumatism created in any kind of proceedings specially in insolvency ones and also the effects of stay of proceedings and others that could affect in one or other way creditors' rights, and even improving time of answer of an enterprise to a crisis. Another possibility would be to allow the possibility of set offs especially in debts between the debtor and financial institutions, maybe under figures similar to factoring or leasing, which would allow the creation of a secondary market of assets of insolvent companies that could, under controlled circumstances increase and create added value to assets of insolvent companies. The possibility of converting debt into equity could also be enhanced, allowing for example external creditors to enter as internal stakeholders, or convert the employees into participants in the company (taking into account that those employees do not have an economic interest only). Moreover, the possibility of payments out of schedule should be allowed for reorganization proceedings (especially for medium / long term obligations), due to the fact that financial situations are not subject to a restrictive schedule.

It is important here to stress that statutory provisions should allow that State owned companies (SOE's) and mixed companies involved in commercial activities should be subject to the general insolvency law with some exceptions, due to the highly controlled economic activity (public services or oil companies for example), this exceptions applying more control over the insolvency procedure; this application could send a message to those companies to tell them that in a liberalized economy they should be

competitive, promoting in that way (a direct message to the management board of such companies) the efficacy in results and reduction of bureaucracy and corruption.

All those legislative changes require long discussions and political consensus, and have to be adopted according to the unique situation of every country.

Finally, I must say that the insolvency systems in Latin America have been having changes, especially after 1998, but still many provisions can be improved and in many countries, the insolvency systems require a structural change. In more specific terms, the countries with an advanced insolvency system are: Argentina, Mexico, Colombia and Brazil; the other countries have insolvency regimes that still have to be improved, being their major problem the rigidity and formality of their provisions, being the worst case the one of Venezuela. The Latin American countries have to be aware that, the new economic and trade realities as I indicated them are there and that if they don't take measures to adapt their insolvency regimes to those new realities, the result can be a crisis of comparable size to the ones lived many times before. It has been an example of this argument that even if it's true that the governments of the Latin American countries are divided between left and right, the leftist governments have taken significant steps towards modernization, contrary to which many people could think<sup>61</sup>. The clock is ticking and the Latin American countries can not ignore its sound: they have to realize that they still have time to change.

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<sup>61</sup> See the case of Brazil with President Luiz I. Lula Da Silva, Chile with President Ricardo Lagos and Argentina with President Nestor Kirchner.

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## **ANNEX I.- DETAILS OF THE INSOLVENCY SYSTEM: ARGENTINA**

### **I.1. REORGANIZATION PROCEEDINGS:**

Referring more in depth to reorganization procedures, which are taken as remedies to avoid liquidation proceedings, it can be mentioned that only a debtor can make a petition for reorganization proceedings, and its petition is taken as a confession for a cessation of payments. In this case, the debtor keeps control of his assets, but is supervised by a “Síndico”, which has a function of control on the debtor and to advise the Court on different matters.

When filling for such a proceeding, the debtor must give reasons for his economic situation, with a detailed report on assets and liabilities, and judicial and administrative processes in which he is involved.

The debtor, once initiated the reorganization proceeding, has an “exclusivity period” (periodo de exclusividad), of 30 to 60 days, in which he can make proposals to creditors for the purposes of the reorganization, offering to them the division in different categories (but always with a component of equality to all inside those categories), or several options to receive their payments. The general rule is that the plans have to be approved by the majority of the creditors and by the Court. If these plans are not approved, the Court has to issue an order of liquidation; however, for corporations and limited partnerships, an exception to this rule exists, consisting of the “salvage” or “Argentine cram down” (salvataje), in which creditors and third parties can purchase the company or the debtor participation on it (according to the case) and eventually, pay the remaining debts of the company.

If a reorganization plan is approved, its main effects is that all the obligations will be novated, meaning that according to the plan, all obligations could change its form, time limits, and conditions.

In the other hand, a creditors’ committee (comité de acreedores) in this proceeding has a function of information and counsel, and specially the function to supervise that the debtor meets the commitments made in the reorganization plan.

### **I.2. INSOLVENCY PROCEEDINGS:**

The jurisdiction for this proceeding is entitled to provincial judges<sup>62</sup>. The main purpose of this procedure is the liquidation of the debtor’s assets. The liquidation petition can be

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<sup>62</sup> For more detailed information about Argentinean insolvency matters please check: “Rules of International Private Law, Priorities on Insolvency and the Competing Right of Foreign and Domestic Creditors, under the Argentine Insolvency Law”

filed by the debtor or a creditor; the liquidation procedure can also be started if the reorganization procedure fails.

In this procedure, the company or debtor loses control over the assets, which pass to be controlled by the liquidator (sindicó) and this person is in charge of selling the assets to pay the liabilities and debts of the company. As a consequence, the company ceases to exist.

The consequences for the directors of the company (debtor) can be several, if mismanagement under a certain degree is proved: 1) Personal disqualification. 2) Legal obligation to compensate losses with their own assets. 3) Personal bankruptcy of the administrators.

The payments to creditors in this proceeding are made according to the ranking mentioned above, from a statement made by the debtor.

Something different than in other Latin American countries is the payment of the debts in a special “currency”, called “bankruptcy money” (moneda de quiebra), meaning the local currency which creditors receive, depending on their priorities in the distribution.

## **ANNEX II.- DETAILS OF THE INSOLVENCY SYSTEM: BRAZIL**

### **II.1. JUDICIAL REORGANIZATION PROCEEDING:**

This procedure aims to make viable the recovery of the debtor of the economical and financial situation that he is facing; keeping the productive sources, the employment of the workers of the debtor, the interests of the creditors; promoting the enterprise, its social function, and promoting the economic activity.

The conditions laid down in the new insolvency law to access the mechanism of reorganization are several, related mostly to ensure avoiding an abuse of the mechanism, with conditions like time to use the mechanism (to file for the first time and a time between one petition and another one). The credits subject to reorganization are all the credits existent up to the date of the filling of the petition of reorganization, if they are not expired, and the creditors keep all their privileges arising from the credits.

Under this proceeding, the reorganization can consist in different forms: reorganization related to the company and its structure as such, and reorganization related to its credits. Therefore, can consist in the novation of the credits (changing its form, time limit, conditions, etc), or the changing the structure of the company (merge, acquire, split the company), the substitution of the members of the social organs or the directors of the company, the issuance of bonds or stocks, etc.

The insolvency proceedings can be ordered by a Court if: 1) the debtor has failed to comply with any obligation in the reorganization plan, 2) the reorganization plan has been rejected, 3) the Creditors' General Assembly has decided so, or 4) if the reorganization plan is not presented within the procedural term to the Court (that have to be delivered to the Court by the debtor in a term of 60 days after the issuance of the decree accepting the proceeding).

The judicial administrator in this proceeding has the following functions: keep the creditors informed of all the proceedings and, in general to collaborate with the creditors to solve any problems arising, also to ask for any necessary information to the parties involved in the proceeding, elaborate the relations of credits and creditors and the final table of creditors, ask the Court to call the Creditors' General Assembly, supervise the debtor to comply with the reorganization plan and if he doesn't to ask the Court to declare the opening of insolvency proceedings, and present periodic information to the Court.

The Creditors' Committee in this proceeding has the following functions: supervise the judicial administrator, communicate to the Court if any violation of the law is found during the proceeding, request the Court to call the Creditors' General Assembly, supervise the activities of the debtor and the compliance with the reorganization plan, etc.

The Creditors' General Assembly in this proceeding has the following functions: approve, reject or modify the reorganization plan, select the Creditors' Committee, and other issues of interest for the creditors.

In the case of extra judicial reorganization, the debtor can make private arrangements with his creditors in order to pay his debts, subject, in general terms, to the approval of the reorganization plan by the Court.

## **II.2. INSOLVENCY PROCEEDING:**

The procedure aims to remove the debtor of his activities, to preserve and optimize the productive use of his assets. Like other proceedings I mention in this paper; the proceeding is initiated due to the incapacity of the debtor to pay its debts, including also carrying out illegal maneuvers to avoid payments or to hide its real situation, and finally, the failure to comply with the reorganization plan in a reorganization proceeding.

In this proceeding, the debtor is deprived of the control of his assets, which pass to be managed by a judicial administrator or liquidator (Síndico), and who also has the function to represent the mass of assets involved in the insolvency proceeding. However, the debtor can still intervene in the insolvency proceeding, and supervise the handling of the proceeding, in order to preserve or defend his rights or interests, and also has the duty to cooperate in all terms with the parties involved in the proceeding.

The decree of insolvency determines the expiration of all debts and obligations of the debtor, and specially, the credits in foreign currency are converted to local currency at the exchange rate of the issuance of the decision; also, if the debtor is conformed by unlimited liability partners, the decree affecting the debtor automatically affects also those partners, with the same legal effects.

The functions of the judicial administrator in this proceeding are: present reports to the Court, keep informed to creditors of all the proceeding, represent the assets of the debtor and practice all the conservation and interim measures to preserve the assets.

The functions of the Creditors' Committee and of the Creditors' General Assembly in this proceeding are actually the same than the mentioned in the reorganization proceeding.

## **ANNEX III.- DETAILS OF THE INSOLVENCY SYSTEM: CHILE**

### **III.1. REORGANIZATION PROCEEDING:**

As I mentioned above, the reorganization proceedings in the Chilean legislation are of two kinds: the simply judicial agreement (*convenio simplemente judicial*), and the preventive judicial agreement (*convenio judicial preventivo*). The first one is presented during the process of bankruptcy, while the latter is presented before the declaration of bankruptcy. The decisions for both of the procedures have to be agreed in the Creditors' General Assembly (*Junta de acreedores*).

Now, referring to the simply judicial agreement, the debtor or any creditor can make the proposition to initiate it in any stage during the bankruptcy proceeding, with the condition that the debtor has not been condemned before for any fraudulent bankruptcy, and that the table of recognized credits and creditors have already been presented by the receiver, once the agreement is approved, the assets of the debtor will return under his control, and he will be subject to supervision of compliance with the approved plan by the receiver and by the creditors. In the other hand, for the preventive judicial agreement, can be applied by the debtor if he has not been condemned of fraud and before his creditors, which have to accept the plan presented by unanimity, and appoint a receiver.

There are some interesting provisions, like that the creditors' General Assembly can, in order to be represented in certain legal acts, appoint a Creditors' Committee; or that the creditors living abroad and not represented in the Creditors' General Assembly will be presumed to be opposed to the agreement (negative vote). Despite all this, the legislation is almost full of procedural steps to follow, which makes the process very slow in practical terms.

### **III.2. INSOLVENCY PROCEEDING:**

As in the other countries referred in this paper, the bankruptcy proceeding aims to execute in a single process the assets of a person to pay his debts. The Chilean law doesn't make any reference to other aims or philosophical objectives of the proceeding, like the legislation of other countries, which makes me think that the aim is purely economic, and doesn't have other objectives like conservation of productive assets or of employment.

The petition to star an insolvency proceeding can be filed by the debtor or any creditor (as I mentioned before), in which has to present a relation of credits, assets, other liabilities and legal procedures in course in the moment of the petition.

The suspension of payments is not, like in other States, the date of the file of the petition (or a *de facto* situation), but it has to be declared in the Decree of the Court declaring the

bankruptcy, and can not be one day before the aforementioned Decree or more than a year later than it.

The Decree declaring the bankruptcy has the effect of removing the debtor of the administration of his assets, and mentions the creditors and their credits and positions, also, all the proceedings against the debtor are accumulated to the bankruptcy proceeding. Also it suspends all the individual proceedings against the debtor, except the ones with a right in rem or privileged that can continue individually.

## **ANNEX IV.- DETAILS OF THE INSOLVENCY SYSTEM: COLOMBIA**

### **IV.1. REORGANIZATION PROCEEDINGS:**

In Colombia there are two (2) reorganization proceedings: the Concordat (law 222/95) and the Restructuration Agreement (Law 550/99).

Although both proceedings have the same effect, that is to recover the debtor to continue its productive activity, there are some differences. Both methods bind all the creditors.

The restructuration agreement is applicable to all legal persons, of public or private nature, foreign or national, that acts as trader or doing trading acts considered as such by law; with the exception of special companies like the ones in the financial sector or others with a special reorganization regime.

The reorganization proceeding can be initiated by the debtor, his creditors or by the Superintendences ex officio, and it is negotiated by the internal and the external creditors of the debtor. The main requirement to apply for a restructuration agreement is the no payment of 2 or more obligations of the debtor for more than ninety (90) days or the existence of two (2) or more executions in course of trading obligations. Those obligations have to be superior to the 5% of the credits of the debtor.

The Superintendence is the one in charge of designating a natural person to act as the promoter of a restructuration agreement, when accepting the request to initiate the proceeding. The promoter can examine the books of the debtor, propose restructuration formulas, determine the voting rights of the creditors and serve as a conciliator between debtor and creditors when negotiating an agreement.

The restructuration agreement negotiation can't pass of four (4) months, during which can't initiate executions against the debtor and the ones in course have to be suspended; in the same manner, the prescription term of the actions against the debtor is suspended. The voting rights of creditors are in accordance of the amount of the credit, but the tax and other public authorities have a preference in the voting rights due that their voting rights are composed of capital and interest, which doesn't happen with other creditors. The agreement has to be approved by an absolute majority of votes, coming from a plurality of creditors.

In the event of failure to conclude an agreement, there can be an initiation of a concordat, or the initiation of a liquidation proceeding.

For the surveillance of restructuration agreement, the creditors can appoint a surveillance committee (Comité de Vigilancia). Composed by representatives of different classes of creditors.

Now, referring to the Concordat, the debtor has to ask its initiation to the respective Superintendence or Court according to the case, with the authorization of the highest social Board (mostly the Shareholders' General Assembly or the Partners' Board). The Superintendence then has to appoint a receiver (Contralor) and a Provisional Creditors' Board (Junta Provisional de Acreedores), communicate to creditors the initiation of the procedure and order the embargo of the assets of the debtor. In addition, no execution process can be initiated, and the ones in course have to be sent from the Judges to the Superintendence in charge.

The receiver is appointed to inform the Superintendence and creditors of the settlement formula, to check the viability of the debtor. His functions will cease when the concordat agreement is approved.

The concordat agreement is approved with the vote in favor of the 75% of the amount of credits recognized.

#### **IV.2. LIQUIDATION PROCEEDING:**

The mandatory liquidation proceeding can be requested by the debtor or ex officio by the Superintendence of Companies.

Once the liquidation proceeding is accepted, the management of the debtor will be removed, all the obligations of the debtor will be triggered and immediately demandable, the dissolution of the legal person is ordered, and all the execution processes are accumulated to the liquidation proceeding. In addition the Superintendence has to appoint a Liquidator (Liquidador), which will be the legal representative of the mass to liquidate, and an Advisory Board to the Liquidator (Junta Asesora del Liquidador), with representatives of the creditors.

## **ANNEX V.- DETAILS OF THE INSOLVENCY SYSTEM: MEXICO**

### **V.1. CONCILIATION PHASE:**

During this stage, the debtor remains in possession of his assets and can continue operating the business in its ordinary way. Interests over debts are suspended, except the ones for debts secured with rights in rem or privileged.

This stage is also privileged by the law, because the next stage, liquidation, is only started if the reorganization of the debtor is impossible.

The period for the debtor to be reorganized is of one hundred and eighty five (185) days, which can be extended for 2 periods of ninety (90) days upon request of the conciliator or creditors and debtor.

The conciliator is a third party appointed by the Institute to try to reach an agreement between creditors and debtor, or if it's not possible, to request the Court to initiate liquidation proceedings. Also has the function to file before the Court the final creditors' list.

The plan reached in this proceeding is binding to dissenting minorities, which also can object the plan.

As for the tax and labor claims, those are stayed in this proceeding, and the debtor can introduce a guarantee to support tax or labor credits and the tax authorities are empowered to negotiate to reach a payment plan.

### **V.2. LIQUIDATION PROCEEDING:**

This stage is entered when the debtor requests to enter directly in the liquidation proceeding, or when there is no agreement for a reorganization plan, or when the period of conciliation has expired, or the conciliator request so to the Court or, finally, if the reorganization plan is not viable.

Once the liquidation stage is started, the assets of the debtor pass to be managed by a trustee.